Supreme Court, U.S.
FILED

NOV 15 2010

IN THE OFFICE OF THE CLERK

No. 10-10-653

Supreme Court of the United States

PSKS, INC. D/B/A KAY'S KLOSET...KAY'S SHOES,
Petitioner,

v.

LEEGIN CREATIVE LEATHER PRODUCTS, INC.,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

In *Leegin*, this Court overruled the per se rule against vertical minimum price-fixing. On remand, Petitioner alleged all the rule-of-reason factors held relevant in *Leegin*, but the Fifth Circuit nonetheless dismissed the complaint, raising legal conflicts on the following important questions.

1. Can economic proof of market definition and power be rejected based on noneconomic formalistic assertions that (a) one brand cannot be a relevant market without buyer lock-in, (b) wholesale markets cannot be separate from retail markets, and (c) market power cannot be proven directly without showing a large market share on a defined market?

2. Does an absolute market-power screen apply to vertical restraints, making it necessary to prove market power even when there is direct evidence of anticompetitive effects, widespread use by competing manufacturers, retailer pressure, and a provable lack of procompetitive justifications?

3. Does failure to make an argument that was irrelevant under then-prevailing precedent waive the right to raise that argument on remand after the precedent is overruled in a way that makes the argument relevant for the first time?

4. Are agreements restraining retail distribution subject to stricter than normal rule-of-reason scrutiny when they involve horizontal agreements (a) between competing independent retailers and (b) between those retailers and a manufacturer who also competes at retail?

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

The parties to this proceeding are PSKS, Inc. d/b/a Kay's Kloset . . . Kay's Shoes (hereinafter referred to as "PSKS" or "Petitioner") and Leegin Creative Leather Products, Inc. (hereinafter referred to as "Leegin"). In addition, Toni Cochran, L.L.C., d/b/a Toni's was included as a plaintiff below.

Pursuant to Supreme Court Rule 29.6, the undersigned counsel certify that Petitioner PSKS, Inc. d/b/a Kay's Kloset...Kay's Shoes is a wholly owned corporation and that no publicly held company owns ten percent or more of its stock.

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PETITION FOR A WRIT OF CERTIORARI

PSKS petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit.

OPINIONS BELOW

The Court of Appeals decision for which review is sought is reported at 615 F.3d 412, which affirmed the District Court opinion at 2009 WL 938561. Earlier orders in the case, for which review is not sought, appear at 2004 WL 5254322, 171 Fed.Appx. 464, and 498 F.3d 486.

JURISDICTION

The Court of Appeals' judgment was entered August 17, 2010. This Court has jurisdiction under 28 U.S.C. §1254(1).

STATUTORY PROVISION INVOLVED

Sherman Act §1, 15 U.S.C. §1, provides: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal."

STATEMENT OF THE CASE

In the initial litigation, the lower courts held that the agreements on retail prices were per se illegal under *Dr. Miles Medical v. John D. Park & Sons*, 220 U.S. 373 (1911). This Court reversed and remanded, overruling *Dr. Miles* and holding that: "Vertical price restraints are to be judged according to the rule of reason." *Leegin Creative Leather Products v. PSKS,*

Inc., 551 U.S. 877, 907 (2007). *Leegin* emphasized that such rule-of-reason review must be "diligent" to eliminate any anticompetitive restraints. *Id.* at 897. *Leegin* also made clear that the premise for applying the rule of reason, rather than a per se rule, was the existence of procompetitive justifications. *Id.* at 889-92. *Leegin* explained that possible relevant factors under the rule of reason included market power, whether competing manufacturers used similar restraints, and whether the restraints reflected retailer pressure. *Id.* at 897-98. *Leegin* also stressed that per se illegality remained applicable when agreements on retail prices involved horizontal agreements among retailers. *Id.* at 893.

On remand, PSKS amended the Complaint to add the factors that *Leegin* held relevant, including market power, widespread use by competing manufacturers, retailer pressure, agreements among competing retailers, lack of procompetitive justification, and direct evidence of anticompetitive effects. The following allegations must be presumed to be true at this stage.

Allegations on Market Definition and Power. "Because Leegin offers products that are highly differentiated, it has market power." Second Amended Complaint ("SAC") ¶17. Leegin's Brighton line is "the only major accessories line featuring products that coordinate from head to toe." SAC ¶16.

> Brighton-brand products are unique. Many customers do not consider other accessories suitable substitutes for their use of Brighton-brand products, nor would they substitute other accessories for Brighton-brand products, nor would they do so even in response to a *significant, non-transitory increase in the price* of Brighton-brand products.

> Brighton-brand products are distinct products characterized by an *inelasticity in demand*, and *little cross-elasticity* of demand between Brighton-brand products and demand for competing products.

SAC ¶¶25-26 (emphasis added). Accordingly, "the retail market for Brighton women's accessories" is a relevant product market, and Leegin "had a substantial market power" in this market, including a 100% market share. SAC ¶24.

"Leegin also has market power because it occupies a dominant position as supplier to independent women's specialty stores." SAC ¶18. Leegin thus had a dominant market share and market power in the market for "the wholesale sale of brand-name women's accessories to independent retailers." SAC ¶24.

Allegations on Effects, Justifications, and Widespread Use. Direct evidence of anticompetitive effects exists because the "Prices paid by consumers of Brighton-brand products were maintained at artificially high and anti-competitive levels." SAC ¶27. Further, "Defendant exercises its market power to limit or discourage the sales by stores of products by new entrants." SAC ¶31. Finally, the Complaint alleges the "wide-spread adoption" by competing manufacturers of similar limits on retail price competition. SAC ¶32.

The restraints on retail price competition here have *no* procompetitive justification because:

> The products at issue do not require service, instruction, or other post-sale aspects that would be likely to be underprovided in the absence of a pricing restriction; the use of pricing restrictions in this case serve to restrict and does not

> enhance entry into the market; to the extent that any services are required to be offered by retailers, those services could be required directly, such that the incentives created by a price fixing scheme are not a more efficient means of achieving the results....

SAC ¶31.

Allegations on Horizontality. Leegin operated retail stores in horizontal competition with independent retailers. SAC ¶¶ 8, 29. Thus, Leegin's agreements with independent retailers to fix retail prices restrained competition between horizontal competitors.

Independent retailers also horizontally conspired amongst themselves to fix retail price terms and pressured Leegin to fix retail prices in particular ways. It was "at the insistence of many of its most faithful retail dealers" that Leegin set many terms of the retail price-fixing agreements and began enforcing them with greater regularity. SAC ¶13. Leegin repeatedly amended the retail price-fixing agreement "following the suggestion and concurrence of retail dealers" acting collectively, including one instance when the retailers met together and reached a "consensus" that restricted discounts to "1 piece of merchandise" on a customer's birthday and explicitly covered "everything not only Brighton" and thus restricted *inter*brand discounting on rival manufacturers' products. SAC ¶14. Leegin "frequently intervened to reconcile pricing disputes between competing retailers" by trying to "work up some agreement" between the retailers. SAC ¶15. "[T]he price fixing scheme facilitates the organization and operation of a retail cartel in the sale of these goods." SAC ¶31. The purpose of agreeing to fix retail prices was so

"Defendant can insulate the retail stores it owns or controls from price competition and protect retailers who have cartelized from price competition from more innovative and efficient retailers." SAC ¶22.

Fifth Circuit Holdings. Rather than applying the "diligent" scrutiny required by *Leegin*, the Fifth Circuit dismissed these allegations out of hand. It held that proving the allegations would not establish market definition or market power, that direct evidence of anticompetitive effects and a provable lack of procompetitive justifications did not suffice without proof of market power, and that the alleged horizontal aspects of the agreement on retail prices were waived and did not trigger stricter antitrust scrutiny. All of these holdings resolved questions of federal law in a way that conflicts with other federal appellate decisions.

REASONS FOR GRANTING THE PETITION

I. THE CONFLICT ON MARKET DEFINITION AND POWER

The Fifth Circuit holding on market definition and power rested on the legal premise that economic proof of low cross-elasticity and price-responsiveness does not suffice to prove market definition or power. Instead, the Fifth Circuit rejected such economic proof based on formalistic, noneconomic doctrines that one brand cannot be a relevant market without buyer lock-in, that wholesale markets cannot be separate from retail markets, and that market power cannot be proven directly without showing a large market share in a defined market. This raises a general legal conflict about whether courts can reject economic proof as a basis for defining markets and

proving market power, as well as legal conflicts on each of the three noneconomic doctrines the Fifth Circuit invoked.

A. The Conflict About Single-Brand Markets

As one of three alternative grounds for finding market power, the Complaint alleges that Brighton-brand products constitute a relevant market because they are unique in offering coordinated head-to-toe accessories for which demand and cross-elasticities are so low that Leegin could impose a small but "significant non-transitory increase in price" (SSNIP) without driving away consumers. SAC ¶¶24-26. The Fifth Circuit held those allegations insufficient, reasoning that "a single brand of a product or service can constitute a relevant market" *only* when "consumers are 'locked in' to a specific brand by the nature of the product." 615 F.3d at 419. This holding conflicts with rulings by this Court and several circuits, whose tests for finding a single-brand market do not make lock-in necessary but do make the SNIPP test or low cross-elasticity sufficient.[1]

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[1] Although the Fifth Circuit stated that the proposed market did not "recogniz[e] the cross-elasticity of demand for Brighton goods," 615 F.3d at 418, we must presume the Fifth Circuit did not improperly ignore the express allegation that there was "little cross-elasticity of demand" between that brand and others. SAC ¶¶25-26. The only way to square the actual allegations with the Fifth Circuit statement is to interpret its statement as implicitly holding that *any* cross-elasticity between one brand and another suffices to defeat market definition, so that an allegation of "little" cross-elasticity does not suffice to prove a relevant market. This holding thus boils down to the same mistaken conclusion that (absent absolute lock-in) one brand cannot be a relevant market as a legal matter regardless of what

The D.C. Circuit held that a merged Whole Food-Wild Oats brand would have a 100% monopoly in eighteen cities as the only provider of premium, natural and organic supermarkets, even though that brand of supermarkets competed in a broader differentiated market with conventional supermarkets. *FTC v. Whole Foods*, 548 F.3d 1028, 1032, 1037–41 (D.C.Cir. 2008) (Brown, J); *id.* at 1043-49 (Tatel, J.). The D.C. Circuit relied on evidence that a SNIPP test showed core buyers would not switch to conventional supermarkets in response to a small price increase. It sufficed that those buyers found the brand characteristics "'uniquely attractive'" enough not to switch in response to small price increases, even though that unique attraction was not based on lock-in. *Id.* at 1039 (Brown, J.) (quoting *NCAA v. Board of Regents*, 468 U.S. 85, 112 (1984)). The Fifth Circuit decision that, despite satisfying the SNIPP test, one brand cannot constitute a relevant market absent evidence of lock-in directly conflicts with the D.C. Circuit's holding that the merged brand would be the relevant market in those eighteen cities. As the D.C. Circuit recognized, what matters is whether the power to raise prices actually exists given buyer preferences, not whether that power is enjoyed by one brand or whether lock-in makes switching to functional alternatives impossible. *See also FTC v. Staples*, 970 F.Supp. 1066, 1073-81 (D.D.C.1997) (price data satisfying the SNIPP test proved that a merged Staples-Office Depot brand would have a 100% monopoly in fifteen cities as the only office superstore, even though that brand of store operated on a

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the economic data show. Moreover, however the Fifth Circuit characterized the complaint, its actual holding is necessarily that the actual allegations did not suffice.

broader differentiated market with other types of stores that sold identical office supplies).

The Fifth Circuit also conflicts with Third and Sixth Circuit decisions that make uniqueness and lack of reasonable interchangeability sufficient to define one brand as a relevant market, without making lock-in a necessary element. *Queen City Pizza v. Domino's Pizza*, 124 F.3d 430, 439 (3d Cir. 1997) ("a single brand of a product or service may constitute a relevant market...where the commodity is unique, and therefore not interchangeable with other products."); *Edward J. Sweeney & Sons v. Texaco*, 637 F.2d 105, 117 (3d Cir. 1980) ("To establish that Texaco gasoline alone constituted a relevant market or submarket, appellants had to prove that Texaco gasoline was not considered reasonably interchangeable with other brands of gasoline and non-branded gasoline by a significantly large number of consumers."); *Tarrant Service v. American Standard*, 12 F.3d 609, 614 (6th Cir. 1993) ("Clearly, one brand of a product can constitute the relevant market when the product is unique and no reasonable substitutes exist."). The Sixth Circuit has also specified that assessing interchangeability for alleged one-brand markets turns on cross-elasticity and the SNIPP test. *Kentucky Speedway v. NASCAR*, 588 F.3d 908, 917-918 (6th Cir. 2009) (using cross-elasticity and the SNIPP test to assess whether NASCAR-brand premium-stock-car races constitute a relevant market).

Also conflicting is a Seventh Circuit decision by Judge Posner that "the manufacturers of brand name prescription drugs engage in price discrimination, showing that they have market power," and "[i]t would not be surprising...if *every* manufacturer of brand name prescription drugs had some market

power." *In re Brand Name Prescription Drugs Antitrust Litigation*, 186 F.3d 781, 786-87 (7th Cir. 1999). This was true despite the absence of lock-in or patent, and even if the brand-name drugs had physically identical "generic substitutes" or "a therapeutically close substitute" with a less familiar brand name, because

> the physicians who prescribe the drug may continue to prescribe the branded version rather than the generic substitute, whether out of inertia, or because they think the branded version may be produced under better quality control (the rationale for trademarks), or because the patient may feel greater confidence in a familiar brand. The same thing is true if the original brand...now has a therapeutically close substitute sold under a brand name that is less familiar to physicians or patients than the original brand.

Id. at 787. In short, the Seventh Circuit recognizes that market power turns on actual buyer willingness to substitute, as captured by cross-elasticity and the SNIPP test, rather than on formalisms such as whether a brand's low cross-elasticity was created by lock-in. Likewise in conflict with the Fifth Circuit is an Eighth Circuit holding that urology services at "a single hospital may constitute the relevant market" even though there is a larger market for urologists' services, without making lock-in a necessary element. *Flegel v. Christian Hospital*, 4 F.3d 682, 690 (8th Cir. 1993).

The Fifth Circuit also conflicts with this Court's decisions. In *Eastman Kodak v. Image Technical Services*, 504 U.S. 451 (1992), this Court held that one brand constitutes a relevant market whenever

other brands are not reasonably interchangeable given low cross-elasticities and that lock-in was just one way of showing other brands were not reasonably interchangeable:

> Kodak also contends that, as a matter of law, a single brand of a product or service can never be a relevant market under the Sherman Act. We disagree. The relevant market for antitrust purposes is determined by the choices available to Kodak equipment owners. *See Jefferson Parish*, 466 U.S. at 19. Because service and parts for Kodak equipment are not interchangeable with other manufacturers' service and parts, the relevant market from the Kodak equipment owner's perspective is composed of only those companies that service Kodak machines. *See Du Pont*, 351 U.S. at 404 ("The market is composed of products that have reasonable interchangeability"). This Court's prior cases support the proposition that in some instances one brand of a product can constitute a separate market. *See NCAA*, 468 U.S. at 101-102, 111-112; *International Boxing Club of New York, Inc. v. United States*, 358 U.S. 242, 249-252 (1959); *IBM v. United States*, 298 U.S. 131 (1936). The proper market definition in this case can be determined only after a factual inquiry into the "commercial realities" faced by consumers. *United States v. Grinnell Corp.*, 384 U.S. at 572.

Kodak, 504 U.S. at 481-82.

The cases that *Kodak* cited to show that "[t]his Court's prior cases support the proposition that in some instances one brand of a product can constitute a separate market" did not involve situations where buyers were locked in to that brand. Further, the

cases that *Kodak* stated provided the appropriate method for determining whether one brand constituted a relevant market were all cases holding that the test turned on demand or cross elasticity, rather than requiring an absolute functional lock-in. The cited part of *Jefferson Parish* held that "whether one or two products are involved turns *not* on the functional relation between them, but rather on the character of the demand for the two items." 466 U.S. at 19 (emphasis added). The cited part of *du Pont* emphasized that the test was "reasonable interchangeability," and *du Pont* elsewhere emphasized that reasonable interchangeability turns on cross-elasticity. 351 U.S. at 380 ("Every manufacturer is the sole producer of the particular commodity it makes but its control in the above sense of the relevant market depends upon the...cross-elasticity of demand."); *id.* at 394 ("What is called for is an appraisal of the 'cross-elasticity' of demand...."). *Kodak* also emphasized it was erroneous to think that "*du Pont* rejected the notion that a relevant market could be limited to one brand," stating that *du Pont* simply held that "one brand does not necessarily constitute a relevant market if substitutes are available." 504 U.S. at 482 n.30. The cited portion of *NCAA* concluded that NCAA football games were a relevant market, rejecting the argument that an ability to switch to other programming (i.e., lack of lock-in) showed the contrary, because NCAA games were "uniquely attractive to advertisers" as evidenced by advertisers' willingness to pay a "premium price" for the qualities differentiating viewers of NCAA football. 468 U.S. at 111-12. The cited part of *International Boxing Club* held that greater consumer demand for championship boxing matches meant they were not reasonably interchangeable with other

professional boxing matches, even though the matches were physically identical and no lock-in dictated those consumer preferences. 358 U.S. at 249-52. The cite to *Grinnell* emphasized that market definition turned on the "commercial realities" of buyer demand. 384 U.S. at 572.

The Fifth Circuit decision thus conflicts with not only *Kodak*, but all the above Supreme Court opinions. It also conflicts with *Brown Shoe v. United States,* 370 U.S. 294, 325 (1962), which held that "The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it." Further, *Brown Shoe* held that "within this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes. The boundaries of such a submarket may be determined by examining such practical indicia as...the product's peculiar characteristics and uses,...distinct customers, distinct prices, sensitivity to price changes, and specialized vendors." *Id.* The Fifth Circuit refused to consider even the low cross-elasticity that *Brown Shoe* held must be used to determine reasonable interchangeability and define the broadest market, let alone the allegations of uniqueness, price-sensitivity, and specialized vendors and customers that *Brown Shoe* held must be considered in assessing the existence of a submarket within a broader market.

B. The Conflict About Wholesale Markets

As an alternative to a single-brand market, Petitioner alleged a market defined as "the wholesale sale of brand-name women's accessories to independent

retailers." SAC ¶24. The Fifth Circuit rejected this market definition, holding: "'Wholesale sale' does not adequately define the relevant market, because the relevant market definition must focus on the product rather than the distribution level." 615 F.3d at 418. In fact, the distribution level is relevant, and the Fifth Circuit offered no rationale for asserting the contrary. Suppose a product has only one manufacturer, who sells only at wholesale to multiple competing retailers, who charge twice the wholesale price to cover their retailing costs. The Fifth Circuit holding means the wholesale market cannot be distinct from the retail market, so that the manufacturer's market share is 33% (its revenue divided by total wholesale and retail revenue), which greatly underestimates its actual monopoly share and power. Retailers' ability to buy the product at retail prices from other retailers is clearly not a reasonable economic substitute for being able to buy the product from a rival wholesaler. Indeed, *Leegin* characterizes agreements between a wholesaling manufacturer and retailers as vertical precisely because they are *not* in the same market, even though they sell the same product.

The Fifth Circuit holding that wholesale provision cannot be a relevant market conflicts with many other circuits. *Schuylkill Energy v. Pennsylvania Power*, 113 F.3d 405, 416 n.14 (3d Cir. 1997) ("The relevant wholesale market in this case...is the sale of energy to PJM member companies and other power pools."); *City of Cleveland v. Cleveland Electric Illuminating*, 734 F.2d 1157, 1166 (6th Cir. 1984) ("the wholesale power market" is a distinct market from "the retail electrical power market"); *Paschall v. Kansas City Star*, 727 F.2d 692, 696 (8th Cir. 1984) (finding "a monopoly in the wholesale metropolitan

daily newspaper market."); *JBL Enterprises v. Jhirmack Enterprises*, 698 F.2d 1011, 1016 (9th Cir. 1983) ("the relevant market existed at the wholesale level" and was defined as "'the sale of beauty products, including but not limited to shampoos and conditioners, to beauty salons and other professional outlets'"); *Ad-Vantage Telephone Directory v. GTE Directories*, 849 F.2d 1336, 1345 (11th Cir. 1987) ("A Section 2 claim can be supported by limiting the market definition to a single level of distribution").

The Fifth Circuit further incorrectly reasoned that a wholesale market for sales to independent retailers could not be a relevant market, even if those retailers were unable to turn to any alternatives, absent evidence that those independent retailers do not compete with chain-store retailers downstream in the distribution of Brighton products. 615 F.3d at 418.[2] This holding ignores the evidence, noted by this Court, that Leegin sells mainly through independent retailers because Leegin deems chain-store retailers inadequate distribution substitutes given their inability to provide the same customer experience, support, or service as independent retailers. 551 U.S. at 882.

Even if evidence about limited downstream substitution did not exist, the relevant market definition inquiry is not whether downstream consumers could switch from independent retailers to chain stores.

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[2] The Fifth Circuit also stated "PSKS has likewise failed sufficiently to allege why Brighton goods are not interchangeable with non-brand name products," 615 F.3d at 418, but made clear this conclusion was irrelevant to its holding, *id.* at n.3, and in any event this statement duplicates the incorrect holding (discussed above) that low demand and cross elasticities do not suffice to show non-interchangeability.

The relevant inquiry is whether the alleged set of *direct* buyers, independent retailers, would switch to non-brand-name women's accessories in response to a small but significant price increase by a hypothetical wholesale monopolist in all brand-name women's accessories. The Fifth Circuit's contrary holding conflicts with many decisions that focus on upstream market power without requiring proven harm to downstream markets. *FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 460–62 (1986) (rejecting objection that no proof existed that upstream denial of x-rays to insurers made downstream dental services more costly); *Mandeville Island Farms v. American Crystal Sugar*, 334 U.S. 219 (1948) (condemning cartel in upstream regional beet market that was unlikely to have any price effect on the downstream worldwide market in refined sugar); *FTC v. H.J. Heinz*, 246 F.3d 708, 719 (D.C.Cir. 2001) (anticompetitive effects in wholesale market suffice despite absence of effect on downstream consumer prices because "no court has ever held that a reduction in competition for wholesale purchasers is not relevant unless the plaintiff can prove impact at the consumer level."); *Telecor Communications v. Southwestern Bell*, 305 F.3d 1124, 1132–33 (10th Cir. 2002) (because allegations concerned upstream market for pay-phone locations, market definition turns on inability of location owners to switch from pay phones to cell phones, even though downstream consumers might find them interchangeable).

C. The Conflict on Direct Proof of Market Power

As a third alternative, Petitioner alleged that, even if the market included all other brands of women's accessories, Petitioner could directly prove Leegin's

market power over price because of product differentiation, demand inelasticity for its brand, and low cross-elasticity with other brands. SAC ¶¶16-17, 24-26. The Fifth Circuit dismissed these allegations, reasoning that "'women's accessories' is too broad and vague a definition to constitute a market. Indeed, it is impossible to imagine that Leegin could have power over such a market." 615 F.3d at 418; *id.* at 417 (market definition necessary to state a claim). The Fifth Circuit holding that market power cannot be proven directly, but rather requires proving market definition and a large market share, raises an express conflict with other circuits that hold market power (indeed even monopoly power) can be proven directly, without having to define a market and show a large market share.

In *Re/Max International v. Realty One,* 173 F.3d 995, 1018 (6th Cir. 1999), the Sixth Circuit stated:

> [A]n antitrust plaintiff is not required to rely on indirect evidence of a defendant's monopoly power, such as high market share within a defined market, when there is direct evidence that the defendant has actually set prices or excluded competition.... This view has been adopted, at least implicitly, in four sister circuits: the First, Eighth, Ninth, and Tenth. *See, e.g., Coastal Fuels of Puerto Rico, Inc. v. Caribbean Petroleum Corp.*, 79 F.3d 182, 196-97 (1st Cir. 1996); *Rebel Oil Co. v. Atlantic Richfield Co.*, 51 F.3d 1421, 1434 (9th Cir.1995); *Flegel v. Christian Hosp.*, 4 F.3d 682, 688 (8th Cir.1993); *Reazin v. Blue Cross & Blue Shield of Kansas, Inc.*, 899 F.2d 951, 966-67 (10th Cir.1990).

Further, the Sixth Circuit *expressly* acknowledged that its view was in conflict with the Fifth Circuit,

stating: "On the other hand, the Fifth Circuit has rejected a plaintiff's claim in light of the defendant's low market share even though there was evidence of control over prices. *See Dimmitt Agri Industries v. CPC International,* 679 F.2d 516, 526 (5th Cir.1982)." *Re/Max*, 173 F.3d at 1019. This Circuit conflict has thus persisted for over a decade despite being explicitly acknowledged by the appellate courts.

The Fifth Circuit also conflicts with the Second, Third, Seventh, and D.C. Circuits, including with opinions by three current justices and three judges who were antitrust professors. *Todd v. Exxon*, 275 F.3d 191, 206-07 (2d Cir. 2001) (Sotomayor, J) ("a threshold showing of market share is not a prerequisite for bringing a § 1 claim. 'If a plaintiff can show an actual adverse effect on competition,...we do not require a further showing of market power.'"); *Allen-Myland v. IBM*, 33 F.3d 194, 209 (3d Cir. 1994) ("'Market share is just a way of estimating market power, which is the ultimate consideration. When there are better ways to estimate market power, the court should use them.'") (quoting *Ball Memorial Hospital v. Mutual Hospital Insurance*, 784 F.2d 1325, 1336 (7th Cir. 1986) (Easterbrook, J.)); *United States v. Baker Hughes, Inc.*, 908 F.2d 981, 992 (D.C.Cir. 1990) (Thomas, J., joined by Ruth Bader Ginsburg, J.) (same); *Toys "R" Us v. FTC*, 221 F.3d 928, 937 (7th Cir. 2000) (Wood, J.) ("the share a firm has in a properly defined relevant market is only a way of estimating market power, which is the ultimate consideration. The Supreme Court has made it clear that there are two ways of proving market power. One is through direct evidence of anticompetitive effects."); *In re Brand Name*, 186 F.3d at 786 (Posner, J.) (finding that market power could be proven by direct proof of price discrimination).

Finally, the Fifth Circuit approach conflicts with sound antitrust economics. IIB Areeda, Hovenkamp, & Solow, *Antitrust* 108 (3d ed. 2007) ("'direct' indicators of market power...can be independent of market definition and are sometimes superior to it.... [M]arket definition may not be necessary to prove market power."); Areeda, *Market Definition and Horizontal Restraints*, 52 Antitrust L.J. 553, 565 (1983) ("Once we know that significant price elevation has occurred and that it is not explained by, say, innovation, we know that the defendant has substantial market power. At that point market definition would be superfluous and irrelevant.... We rely on market definition when we cannot assess power directly."); Easterbrook, *The Limits of Antitrust,* 63 Tex. L. Rev. 1, 22–23 (1984) ("Market definition is just a tool in the investigation of market power; it is an output of antitrust inquiry rather than an input into decisions, and it should be avoided whenever possible"); Farrell & Shapiro, *Antitrust Evaluation of Horizontal Mergers: An Economic Alternative to Market Definition*, 10 B.E. J. Theoretical Econ. Iss. 1 (Policies and Perspectives), Article 9 (2010) (in differentiated markets, proving price effects directly is simpler and more accurate than market definition); Kaplow, *Why (Ever) Define Markets?,* Harvard Olin Center Working Paper 666 (March 2010), forthcoming Harvard Law Review (market definition should be abandoned because direct measures of market power are more accurate); Schmalensee, *Another Look at Market Power*, 95 Harv. L. Rev. 1789, 1800 (1982) ("If substantial differentiation can be demonstrated, market share computation is unlikely to yield reliable information, and other tests must be employed to diagnose the importance of market power.").

II. THE CONFLICT ON A MARKET POWER SCREEN

Petitioner alleged direct evidence of anticompetitive effects on prices and entry, retailer pressure, widespread adoption of similar price restraints by competing manufacturers, and the absence of any procompetitive justification. SAC ¶¶ 13-15, 27, 31-32. The Fifth Circuit held this alleged evidence insufficient, adopting a "market-power screen" that made proof of market power necessary to show a vertical restraint violates the rule of reason. 615 F.3d at 418-19; *id.* at 419 (rejecting alleged direct evidence of higher prices because it could not be true "[a]bsent market power" and rejecting all the effects allegations because none could show "harm to interbrand competition" absent market power); *id.* at 417 (holding lack of procompetitive justification irrelevant absent market definition).

In *Indiana Dentists*, this Court held that, under the rule of reason, direct evidence of anticompetitive effects obviates the need to prove market power:

> Since the purpose of the inquiries into market definition and market power is to determine whether an arrangement has the potential for genuine adverse effects on competition, "proof of actual detrimental effects, such as a reduction of output," can obviate the need for an inquiry into market power, which is but a "surrogate for detrimental effects."

476 U.S. at 460 (quoting 7 Areeda, *Antitrust Law* 429 (1986)). This holding was stated as a general proposition when applying the rule of reason, without distinguishing applications to horizontal or vertical restraints. Moreover, this proposition rests on a

rationale that is equally valid when applying the rule of reason to horizontal or vertical restraints: that anticompetitive effects are what we actually care about and market power is merely an imperfect proxy for effects, so it makes no sense to require evidence of market power when direct evidence of anticompetitive effects exists.

Nonetheless, a circuit split has arisen over whether this proposition applies to vertical restraints. The Fourth and Seventh Circuits have, like the Fifth Circuit, held that proving market power is always necessary to prove a vertical restraint violates the rule of reason. *Republic Tobacco v. North Atlantic Trading*, 381 F.3d 717, 737 (7th Cir. 2004); *Murrow Furniture v. Thomasville Furniture*, 889 F.2d 524, 528 (4th Cir. 1989).[3] In contrast, the Second, Eighth, and Ninth Circuits have held that direct proof of anticompetitive effects obviates the need to prove market power in a vertical restraints case. *K.M.B. Warehouse v. Walker Manufacturing*, 61 F.3d 123, 128–29 (2d Cir. 1995); *Ryko Manufacturing v. Eden Services*, 823 F.2d 1215, 1231 n.14 (8th Cir. 1987); *Oltz v. St. Peter's Community Hospital*, 861 F.2d 1440, 1448 (9th Cir. 1988). This Circuit conflict has now lasted for decades and cannot plausibly be resolved without this Court's intervention.

The Fifth Circuit holding also conflicts with another proposition from *Indiana Dentists,* that:

> Absent some countervailing procompetitive virtue...an agreement limiting consumer choice by impeding the "ordinary give and take of the

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[3] The Fifth Circuit also cited *Graphic Product Distributors v. ITEK*, 717 F.2d 1560 (11th Cir. 1983), but that case came before *Indiana Dentists*.

> market place," cannot be sustained under the Rule of Reason.... [Thus,] "[a]s a matter of law, the absence of proof of market power does not justify a naked restriction on price or output" [but rather] such a restriction "requires some competitive justification even in the absence of a detailed market analysis."

Id. at 459-60 (quoting *National Society of Professional Engineers v. United States*, 435 U.S. 679, 693-95 (1978); *NCAA*, 468 U.S. at 109-110).[4] This holding was stated as a general proposition when applying the rule of reason to any restraint on price or output that was naked of any procompetitive justification, and thus did not distinguish between vertical and horizontal restraints on price or output. Its rationale is also equally applicable whether the rule of reason is being applied to vertical or horizontal restraints. That rationale is that, absent any procompetitive justification, nothing on the positive side of the ledger weighs against any anticompetitive effects, and thus we have no reason to burden courts and litigants with complicated inquiries into the extent of the anticompetitive effects caused by a restraint on free market choice. To the contrary, such burdensome inquiry undermines antitrust deterrence without any offsetting gain.

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[4] *California Dental* later held that the abbreviated rule-of-reason for restraints naked of any justification was inapplicable when (1) the restraint was not directly on price or output *and* (2) anticompetitive effects were not obvious because there was a plausible justification. *California Dental Association v. FTC*, 526 U.S. 756, 769–81 (1999). Here, the restraint is directly on price and the complaint alleges there is no plausible justification. Nor does *California Dental* alter the proposition that direct evidence of anticompetitive effects obviates the need to prove market power.

Finally, the Fifth Circuit holding conflicts with *Leegin* itself, which indicated that no absolute market-power screen applies under the rule of reason this Court adopted to judge vertical price restraints. This Court stated that the applicable rule-of-reason inquiry involved several "[a]ppropriate factors to take into account," including "'specific information about the relevant business' and 'the restraint's history, nature and effect.' Whether the businesses involved have market power is a *further, significant consideration*." 551 U.S. at 885–86 (emphasis added) (citations omitted). When discussing vertical restraints specifically, the Court identified three "relevant," non-exhaustive factors: (1) whether "many competing manufacturers adopt the practice"; (2) whether the practice reflected "retailer pressure," and (3) whether "the relevant entity has market power." *Id.* at 897-98. All the Court said about manufacturer market power was that "if a manufacturer lacks market power, there is *less likelihood* that it can use the practice to keep competitors away from distribution outlets." *Id.* at 897-98 (emphasis added). The above language conflicts with any absolute market-power screen. Further, here Petitioner explicitly alleged the other factors set forth in *Leegin*, including retailer pressure and widespread adoption of similar retail price restraints by competing manufacturers. SAC ¶¶13-15, 32.[5]

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[5] Although PSKS alleged "wide-spread adoption of practices that have the effect of limiting price competition among competing brands," SAC ¶32, the Fifth Circuit stated that PSKS never alleged "RPM is widespread in the relevant market." 615 F.3d at 419. The only way to square the Fifth Circuit statement with the actual allegations is to assume the Fifth Circuit statement relied on its conclusion that "the relevant market"

Moreover, *Leegin* stressed that lower courts should use "presumptions where justified, to make the rule of reason a fair and efficient way to prohibit anticompetitive restraints and to promote procompetitive ones." *Id.* at 899. This language clearly indicates that courts should continue to apply presumptions like the standard rule-of-reason presumptions that direct evidence of anticompetitive effects obviates the need to prove market power and that an absence of procompetitive justification suffices to condemn a restraint on price or output.

III. THE CONFLICT ABOUT WAIVER

Prior to *Leegin,* an agreement on retail prices was per se illegal whether or not it had horizontal aspects. Accordingly, in the initial litigation, it would have been irrelevant for Petitioner to argue that horizontal aspects of the agreement on retail prices made it per se illegal. Thus, although Petitioner did allege those horizontal aspects in the initial litigation,[6] Petitioner did not make the then-irrelevant argument that those horizontal aspects would have triggered per se illegality even without *Dr. Miles.* After *Leegin* overruled *Dr. Miles*, those horizontal aspects became relevant for the first time, and Petitioner on remand argued that those horizontal aspects trigger per se scrutiny even though a purely

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had not been defined and its holding that such market definition was necessary.

[6] *See* First Amended Complaint ¶ 9 (alleging that Leegin not only sells to retailers but also competes with them with its own retail stores); *id.* ¶18 (alleging that Leegin and retailers acted "in combination with each other and competing retailers as part of a conspiracy to protect the other retailers from price competition").

vertical agreement no longer does. Nonetheless, the Fifth Circuit held that, by relying on pre-*Leegin* precedent to avoid making the then-irrelevant argument that the agreement had horizontal aspects, Petitioner waived its right to argue that those horizontal aspects trigger stricter than normal rule-of-reason scrutiny now that *Leegin* has overruled the per se rule on vertical price-fixing. 615 F.3d at 420.[7]

This Fifth Circuit decision conflicts with other circuits holding that a party cannot waive an argument if it had no incentive to raise it under the circumstances of the initial litigation, and can raise that argument later if an intervening appellate decision makes it newly relevant. *United States v. Quintieri*, 306 F.3d 1217, 1229 (2d Cir. 2002) ("An issue is not considered waived, however, if a party did not, at the time of the purported waiver, have both an opportunity and an incentive to raise it....") ; *United States v. Atehortva*, 69 F.3d 679, 685 (2d Cir.1995) (failing to make an argument cannot be viewed as a waiver if that argument would have then been "purely academic" or "superfluous"); *United States v. Ticchiarelli*, 171 F.3d 24, 32-33 (1st Cir. 1999) ("'the district court

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[7] Although the Fifth Circuit called its conclusion on waiver an application of the "mandate rule," that name is inapt because the mandate rule simply provides that lower courts must follow Supreme Court mandates. *Briggs v. Pennsylvania Railroad*, 334 U.S. 304, 306 (1948). *Leegin* never held that, by not raising the then-irrelevant argument that horizontal aspects would have also triggered per se scrutiny, plaintiff waived its right to raise that argument on remand now that the overruling of *Dr. Miles* makes it relevant. *Leegin* simply stated that this Court would not consider that argument before it was first raised below. 551 U.S. at 908 ("Respondent did not make this [horizontal] allegation in the lower courts, and we do not consider it here.")

may consider only such new arguments or new facts as are made newly relevant by the court of appeals' decision'....Whether there is a waiver depends...on whether the party had sufficient incentive to raise the issue in the prior proceedings."); *United States v. Whren*, 111 F.3d 956, 960 (D.C.Cir.1997) ("the district court may consider only such new arguments or new facts as are made newly relevant by the court of appeals' decision.... A defendant should not be held to have waived an issue if he did not have a reason to raise it....").[8] These circuit decisions conflict with the Fifth Circuit's waiver ruling because, in the initial litigation, Petitioner had no incentive or reason to argue that horizontal aspects made the agreements on retail prices per se illegal, as *Dr. Miles* made that argument superfluous. *Leegin* made this argument "newly relevant" by holding that per se illegality no longer applied unless the agreements were horizontal.

The rationale underlying the above decisions is equally applicable and strongly persuasive here. Other circuits have held that to impose waiver in such cases:

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[8] Many other cases similarly hold that failing to make an argument that would have been futile under then-applicable precedent does not waive the right to do so after that precedent is overruled. *Curtis Publishing v. Butts*, 388 U.S. 130, 143-45 (1967); *Hawknet v. Overseas Shipping*, 590 F.3d 87, 92 (2d Cir. 2009); *Bennett v. City of Holyoke*, 362 F.3d 1, 7 (1st Cir. 2004); *Holland v. Big River Minerals*, 181 F.3d 597, 605–66 (4th Cir. 1999); *United States v. Rogers*, 118 F.3d 466, 471 (6th Cir. 1997); *Lauchli v. United States*, 402 F.2d 455, 456 (8th Cir.1968). Here, arguing in the initial litigation that the horizontal aspects made the agreements on retail prices per se illegal would have been futile because that argument was then irrelevant.

> "would unnecessarily increase the burden on district courts and this court" because "[parties] would be forced to litigate every aspect of the [situation] in the original [litigation], even though irrelevant to the immediate...determination in anticipation of the possibility that, upon remand, the issue might be relevant."

Quintieri, 306 F.3d at 1229 (citation omitted); *Ticchiarelli*, 171 F.3d at 32 (same). Likewise, the Fifth Circuit's waiver doctrine unnecessarily increases the burden on courts because it means that, in every case, every party must raise not only arguments that are relevant under existing precedent, but also arguments that are irrelevant but might become relevant if that precedent is later overruled. Such an approach would vastly overcomplicate litigation, forcing courts to resolve many irrelevant issues merely because later decisions might make them relevant someday. Moreover, a party may only waive a "known right or privilege." *Johnson v. Zerbst*, 304 U.S. 458, 464 (1938). During the initial litigation Petitioner could not have known it was waiving a relevant argument on per se illegality by not arguing horizontality, given that *Dr. Miles* made horizontality irrelevant.

The Fifth Circuit decision is even more in conflict with decisions holding that, even if prevailing precedent did not make an argument irrelevant, failing to raise an argument does not waive it if the argument would have merely provided an alternative ground for a conclusion supported by other arguments. *Crocker v. Piedmont Aviation*, 49 F.3d 735, 740–41 (D.C.Cir. 1995); *Loudermill v. Cleveland Board of Education*, 844 F.2d 304, 309–10 (6th Cir. 1988). As *Loudermill* put it:

> The Board...was successful in its claim that due process does not require a pretermination hearing. As such, the Board was certainly not bound to bring up an alternative ground on which its success could be based. Thus, the Board is not now barred from raising a new defense under this argument.

Id. This logic dictates finding non-waiver here, because (to track the above language) in the initial litigation Petitioner

> was successful in its claim that [vertical minimum price-fixing] does not require [proving market power]. As such, [Petitioner] was certainly not bound to bring up an alternative ground on which its success could be based [here, that horizontal elements mean the claim did not require proving market power]. Thus, [Petitioner] is not now barred from raising a new [theory] under this argument.

Moreover, the rationale for these cases is that "forcing [parties] to put forth every conceivable alternative ground...might increase the complexity and scope of [litigation] more than it would streamline the progress of the litigation" and would create "the potential judicial *dis*economies of forcing appellees to multiply the number of arguments presented." *Crocker*, 49 F.3d at 740-41. Again, that rationale is equally applicable here.

The Fifth Circuit cited a Ninth Circuit decision holding that, by not arguing in the initial litigation that agreements restricting retailer territories had horizontal aspects, the plaintiff waived the right to do so after this Court overruled precedent that had made certain vertical territorial restraints per se

illegal. *Continental TV v. GTE Sylvania*, 694 F.2d 1132, 1136 n.6 (9th Cir. 1982). However, in the initial litigation of that case, it was unclear the precedent applied to the restraint at issue; indeed, the Ninth Circuit had held it did not. *Id.* at 1135. Thus, in the initial litigation there, it would have been relevant to argue that horizontal aspects triggered per se illegality. In contrast, in the initial litigation here, *Dr. Miles* clearly applied, so it would have been irrelevant to argue horizontality. In any event, even if the Ninth Circuit decision were read to support the Fifth Circuit, that only makes the circuit conflict more pervasive and accentuates the need for Supreme Court intervention.

IV. THE CONFLICT ABOUT HORIZONTALITY

The Fifth Circuit held that, even if arguments about horizontality were not waived, proving the allegations could not establish that the retail price agreements were horizontal. This holding raises important legal conflicts.

A. The Conflict Regarding Dual Distribution Restraints

The Fifth Circuit rejected the argument that Leegin's retail stores made the retail price agreements between Leegin and independent retailers horizontal, holding that such dual distribution restraints should be treated the same as purely vertical distribution restraints. 615 F.3d at 420-21. There is a pervasive circuit conflict on how to treat dual distribution restraints.

Five circuits agree with the Fifth Circuit that agreements between a retailer and a manufacturer

who also competes at retail are categorically vertical and therefore subject to normal rule-of-reason scrutiny. *Electronics Communications v. Toshiba America*, 129 F.3d 240, 243 (2d Cir. 1997); *AT&T v. JMC Telecom*, 470 F.3d 525, 531 (3d Cir. 2006); *International Logistics v. Chrysler*, 884 F.2d 904, 906 (6th Cir. 1989); *Illinois Corporate Travel v. American Airlines*, 889 F.2d 751, 753 (7th Cir. 1989); *Smalley & Co. v. Emerson & Cuming*, 13 F.3d 366, 368 (10th Cir. 1993).

In contrast, four circuits classify dual distribution restraints as vertical when they serve manufacturer interests, but horizontal when they serve retailer interests. *Donald B. Rice Tire v. Michelin Tire*, 638 F.2d 15, 16 (4th Cir. 1981) (dual distribution restraints should be treated as horizontal and per se illegal if they "benefit the dealers" and as vertical and subject to rule-of-reason scrutiny if they "redound[] primarily to the benefit of the manufacturer"); *Hampton Audio Electronics v. Contel Cellular*, 1992 WL 131169, at *3 (4th Cir. 1992) (citing *Donald B. Rice* for proposition that dual distribution restraints should be classified as vertical and subject to rule-of-reason analysis only if they "'redound[] primarily to the benefit of the manufacturer'"); *Ryko Manufacturing*, 823 F.2d at 1231 (dual distribution restraints should be deemed vertical, with the exception that "When competing distributors conspire with their supplier to impose restrictions that redound primarily to the benefit of the distributors, the agreement should be considered horizontal even though it is vertical in form."); *Krehl v. Baskin-Robbins*, 664 F.2d 1348, 1356–57 (9th Cir. 1982) ("our inquiry focuses not on whether the vertical or horizontal aspects of the system predominate, but rather, on the actual competitive impact of the dual distribution system....

Accordingly, we conclude that, in the absence of proof of anti-competitive purpose or effect, dual distribution systems must be evaluated under the traditional rule of reason standard."); *Midwestern Waffles v. Waffle House*, 734 F.2d 705, 711, 720 (11th Cir. 1984) (whether a dual distribution restraint is horizontal or vertical turns on whether retailers influence the terms of the restraint and whether the restraint "has the tendency to reduce interbrand competition, reduce the availability of services within the relevant market area, or artificially maintain prices").

In the latter circuits, the agreements here would be horizontal because they allegedly serve retailer interests rather than manufacturer interests. Petitioner alleges that "the price fixing scheme facilitates the organization and operation of a retail cartel in the sale of these goods," SAC ¶31, and that the purpose was to "insulate the retail stores [Leegin] owns or controls from price competition and protect retailers who have cartelized from price competition from more innovative and efficient retailers." SAC ¶22. The Complaint alleges further that the manufacturer received no additional retail services or procompetitive efficiencies from the price-fixing agreements. SAC ¶31. To the contrary, the price-fixing agreement deprived Leegin from being able to distribute through the most efficient provider of retail services. SAC ¶22. Leegin nonetheless enforced the price-fixing agreements "at the insistence" of the independent retailers, whom Leegin needed in order to distribute its products. SAC ¶13; 551 U.S. at 882.

The Fifth Circuit reasoned that a dual distributor's sole interest would remain minimizing retail markups. 615 F.3d at 421. But dual distributorship attenuates the manufacturer interest in minimizing retail

markups because the manufacturer enjoys those markups at its retail stores, thus making it easier for retailer pressure to overcome the normal manufacturer interest in low markups. The above allegations, which must be accepted as true, show that Leegin's manufacturer interest in low markups at independent retailers was outweighed by the combination of (a) Leegin's need to maintain sales volume at independent retailers by keeping them happy with inefficiently high markups and (b) Leegin's interest in high markups at its own retail stores. The Fifth Circuit holding that the manufacturer interest in low retail markups eliminates possible anticompetitive incentives conflicts with *Leegin*, which summarized economic literature showing that manufacturers might fix retail prices to serve retailer interests. 551 U.S. at 893. Because the whole reason to treat vertical restraints differently is the manufacturer interest in minimizing markups, the attenuation of that interest in dual distribution restraints justifies subjecting them to stricter than normal rule-of-reason scrutiny, including summary condemnation when, as here, they lack any procompetitive justification.

However this Court wishes to treat dual distribution, some resolution by it is necessary to resolve this circuit split, which has endured for decades.

B. The Conflict Regarding Agreements Among Retailers

The Complaint alleged that retailers "insist[ed]" on several changes to price restraints and more regular enforcement, that competing retailers met together and reached a collective "consensus" that restricted discounts on Leegin's *and rival manufacturer's accesso-*

ries to "1 piece of merchandise" on a customer's birthday, that competing retailers had Leegin "work up some agreement" between them when they had pricing disputes, and that retailers used the retail price agreements to facilitate "the organization and operation of a retail cartel." SAC ¶¶13-15, 31. The Fifth Circuit held that such allegations were inadequate to show horizontal agreements because "PSKS has not alleged that any dominant retailer imposed the RPM policy on Leegin, nor has it alleged an agreement among retailers to implement the RPM policy." 615 F.3d at 420. The Fifth Circuit apparently equated the absence of alleged retailer agreements to "implement" the price restraints with an absence of allegations "that retailers agreed to RPM among themselves," and equated the fact that "implementing" the price restraints was done by the manufacturer after discussions with retailers with a conclusion that the manufacturer was the "source" of the restraint. *Id.*[9]

This holding conflicts with *Leegin*, which stated that a horizontal agreement among retailers would be per se illegal even though those prices were discussed with a manufacturer, who then used vertical price restraints to implement the cartel. 551 U.S. at 893. It also conflicts with many other cases finding horizontal agreements when rivals agree on restraints that are implemented and enforced by a vertically-related firm. *See United States* v. *General Motors*, 384 U.S. 127, 143 (1966) (finding horizontal agreement among dealers to get General Motors to

[9] This reading is the only way to square the holding with the actual allegations, which do allege agreements among the retailers on price restraints and pressure by retailers on Leegin to adopt and enforce price restraints.

reach and enforce vertical agreements with dealers); *Interstate Circuit v. United States*, 306 U.S. 208, 226-27 (1939) (finding horizontal agreement among movie distributors that was implemented through a series of vertical agreements with a movie exhibitor); *Toys "R" Us*, 221 F.3d at 935–36 (finding horizontal agreement by manufacturers to restrict sales to certain stores that was implemented through a series of vertical exclusionary agreements with a buyer). The Fifth Circuit's conclusion that such a horizontal agreement requires a dominant retailer also conflicts with *Toys "R" Us,* which found that evidence of a horizontal agreement made retailer market power irrelevant. *Id.* at 936. It also conflicts with countless cases holding horizontal agreements illegal even if none of the participants is a dominant firm. *See, e.g., Eastern States Retail Lumber Dealers' Association v. United States*, 234 U.S. 600, 609 (1914) (finding horizontal agreement among "hundreds of retailers"). Moreover, here competing retailers agreed to restrict discounts on accessories manufactured by *Leegin's rivals*, a horizontal restriction on *inter*brand competition that could not be implemented solely by Leegin-retailer agreements restricting discounts on Leegin's accessories. *Catalano, Inc. v. Target Sales,* 446 U.S. 643, 648 (1980) (horizontal agreement to restrict discounts per se illegal).

CONCLUSION

Not only does the Fifth Circuit opinion raise circuit conflicts on several important issues, but those conflicts raise a common question of great import: is it proper to replace *Leegin*'s rule of reason with an effective rule of per se *legality*? Given the Fifth Circuit holdings, when a wholesaler agrees on retail prices with its retailers, one can *never* prove a high

market share (because the Fifth Circuit requires putting wholesale and retail sales in the same market as each other and with other brands), and thus one can *never* prove market power (because the Fifth Circuit prohibits finding market power without showing a high market share) or a rule-of-reason violation (because the Fifth Circuit adopts a market-power screen despite direct evidence of anticompetitive effects, lack of justification, widespread manufacturer use, and horizontal retailer agreements). In combination, then, the Fifth Circuit holdings effectively make retail price-fixing per se *legal* if a wholesaler agrees to it. This conflicts with *Leegin,* which required courts to apply diligent rule-of-reason review and to examine precisely the factors that the Fifth Circuit dismissed. It also conflicts with sound antitrust policy because powerful empirical evidence demonstrates that switching from per se illegality to per se legality sharply raises prices to consumers. *See* 551 U.S. at 912-13 (Breyer, J., dissenting, joined by Stevens, Souter, and Ginsburg, JJ., dissenting) (collecting evidence that prices were 19-27% higher in states that allowed vertical price-fixing during the Miller-Tydings Act); Elhauge, *Harvard, Not Chicago*, 3(2) Competition Policy International 59, 61 (Autumn 2007) (observing that this empirical evidence showed that switching to per se *legality* would raise prices, although switching to real rule-of-reason review might not).

Perhaps even more alarmingly, in its zeal to create an effective rule of per se legality for retail price agreements, the Fifth Circuit raised circuit conflicts over general issues of market definition, market power, rule-of-reason review, and ascertaining horizontal agreements. Those conflicts sweep beyond vertical price restraints to disrupt antitrust enforce-

ment on mergers, cartels, monopolization, and all other areas of antitrust. On each topic, the Fifth Circuit violated *Leegin*'s instruction that courts should not base decisions on "'formalistic' legal doctrine rather than 'demonstrable economic effect.'" 551 U.S. at 888. Ultimately, then, the Petition raises an even more fundamental question: will modern antitrust jurisprudence live up to its aspiration of replacing arid formalisms with sound economics, or will it have the more dismal legacy of replacing old pro-plaintiff formalisms with new pro-defendant formalisms equally lacking in economic merit?

The petition for certiorari should be granted.

Respectfully submitted,

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November 15, 2010

APPENDIX

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APPENDIX A

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 09-40506

PSKS, INC., DOING BUSINESS AS
KAY'S KLOSET . . . . KAY'S SHOES,
Plaintiff-Appellant,

versus

LEEGIN CREATIVE LEATHER PRODUCTS, INC.,
Defendant-Appellee.

Appeal from the United States District Court
for the Eastern District of Texas

Before SMITH, GARZA, and CLEMENT, Circuit Judges.

JERRY E. SMITH, Circuit Judge.

PSKS, Inc. ("PSKS"), sued for alleged violations of §1 of the Sherman Act and obtained a substantial judgment. This court affirmed. *PSKS, Inc. v. Leegin Creative Leather Prods., Inc.*, 171 F. App'x 464 (5th Cir. 2006). The Supreme Court reversed, overruling *Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911), and holding that vertical price restraints, like vertical nonprice restraints, often have procompetitive justifications and should be judged under the rule of reason. *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877

(2007) ("*Leegin*"). On remand, we further remanded to the district court for proceedings in light of the Supreme Court's opinion. *PSKS, Inc. v. Leegin Creative Leather Prods., Inc.*, 498 F.3d 486 (5th Cir. 2007) (per curiam). The district court granted defendant's motion to dismiss on the merits. *PSKS, Inc. v. Leegin Creative Leather Prods., Inc.*, No. 2:03-CV-107, 2009 WL 938561 (E.D. Tex. Apr. 6, 2009). We affirm.

I.

A. Factual Background.

Leegin Creative Leather Products, Inc. ("Leegin"), manufactures and dis-tributes handbags, belts, jewelry, and other products under the "Brighton" brand. PSKS operated Kay's Kloset, a retail fashion and accessories store in Lewisville, Texas, that sold Brighton products and goods from other manufacturers to consumers in the greater Dallas area.

Leegin utilizes a "dual distribution system" for its Brighton products. It distributes Brighton goods at the wholesale level to independent retailers through periodic trade shows. It also owns and controls over one hundred Brighton retail stores. The company thus is both manufacturer and retailer.

To harmonize and control the price of Brighton goods, Leegin imposed a resale price maintenance policy. PSKS violated that policy by offering Brighton products at a discount through Kay's Kloset. When PSKS refused to stop discounting Brighton goods, Leegin ceased to sell Brighton goods to it.

PSKS sued Leegin, alleging that it had entered into vertical resale price maintenance ("RPM") agreements. The jury awarded $3,975,000 to PSKS, and this court affirmed pursuant to Dr. Miles. *PSKS, Inc.*

v. Leegin Creative Leather Prods., Inc., 171 F. App'x 464 (5th Cir. 2006).

B. The Supreme Court's Decision.

The Supreme Court granted certiorari to reexamine the *per se* rule of *Dr. Miles*. *Leegin*, 551 U.S. at 881. The Court recognized that the "economics literature is replete with procompetitive justifications for a manufacturer's use of resale price maintenance." *Id.* at 889. It noted that the *per se* rule applies only to restraints that exhibit "manifestly anticompetitive effects" and lack any redeeming virtue. *Id.* at 886. It then held that the *per se* rule is no longer appropriate to RPM arrangements, overruling *Dr. Miles*. *Id.* at 907. Instead, vertical price restraints, like vertical nonprice restraints, must be judged under the rule of reason. *Id.*

The Court reasoned that RPM arrangements can have important pro-competitive effects, such as encouraging retailers to invest in services and promotions and eliminating free riding by discounting retailers. *Id.* at 890-91. The Court nevertheless acknowledged the possible anticompetitive justifications of a RPM regime. Such arrangements can facilitate a manufacturer cartel or a cartel at the retail level. *Id.* at 892-93. In the latter instance, a group of retailers could collude to fix prices to consumers and then convince the manufacturer to aid that unlawful arrangement. A dominant retailer or manufacturer, similarly, could abuse RPM to its advantage. *Id.* at 893. A dominant retailer with an extensive distribution network, for instance, might request RPM to build a moat against competition, and manufacturers might feel compelled to comply in order to access that distribution network. *Id.* at 893-94 (citing *Toys "R" Us, Inc. v. FTC*, 221 F.3d 928, 937-38 (7th Cir. 2000)).

The opinion addressed the common criticism, raised again by PSKS and *amicus* in this appeal, that the rule of reason is tantamount to a rule of *per se* legality. *Id.* at 897-98. The Court overruled *Dr. Miles* and adopted the rule of reason precisely because that standard allows lower courts to weed out anticompetitive RPM without subjecting countless procompetitive uses to drawn out judicial scrutiny. *Id.* at 898-99.

The *Leegin* decision also tore down the artificial doctrinal wall between vertical price and nonprice restraints that had received much criticism after *Continental T. V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977). *Leegin*, 551 U.S. at 904. That was a critical observation, for it permits this court and lower courts to draw upon existing vertical nonprice restraint jurisprudence in RPM cases, provided that application of the rule of reason always requires a case-by-case analysis and that there may be situations in which the anticompetitive effects of vertical price and nonprice restraints will differ.

C. PSKS's claims on remand and the district court's opinion.

On remand, PSKS filed a second amended complaint alleging that independent retailers were involved in the enforcement of Leegin's RPM policy. Specifically, it alleged that at a meeting, more than one hundred of Leegin's most successful retailers had reached a consensus regarding special occasion discounts and enticements and that that consensus was then adopted and announced as company policy by Leegin's president, Jerry Kohl. It further alleged that Leegin was the hub in a hub-and-spoke conspiracy, because it would intervene to resolve pricing disputes between and among competing Brighton

retailers. At the same time, PSKS alleged that Leegin is "the largest single retailer of Brighton products."

PSKS finally claimed that Leegin, acting at the retail level, agreed with other retailers on the price at which Brighton goods would be sold to consumers. It therefore alleged that Leegin was involved in a horizontal price-fixing conspiracy. PSKS did not allege that retailers were the "source" of the RPM policy or that Leegin established the policy at retailers' behest. Nor did it allege any agreement among retailers or between Leegin and competing manufacturers. The second amended complaint alleged four anticompetitive effects: (1) that consumers were made to pay an artificially high price for Brighton products; (2) that consumers were "deprived of free and open competition in the purchase of Brighton-brand products"; (3) that PSKS was hindered in its efforts to buy "competing products"; and (4) that consumers were "forced" to pay artificially high and anticompetitive prices for Brighton products.

PSKS also urged that the rule of reason is inapplicable to Leegin's conduct, because Leegin is a dual distributor. PSKS consistently alleged that RPM ar-rangements must be analyzed differently in dual distribution settings from how they are analyzed in the more common instance in which the manufacturer does not participate at the retail level.

PSKS alleged the relevant product markets as: (1) the "retail market for Brighton's women's accessories" and (2) the "wholesale sale of brand-name women's accessories to independent retailers." It additionally claimed that Leegin had market power based on its "highly differentiated products," its large showroom at the Dallas trade show, and its alleged

position as the largest among an unspecified number of manufacturers in the proposed wholesale market.

The district court dismissed PSKS's second amended complaint, holding that it had failed to plead a plausible relevant market as required under the rule of reason; that its new horizontal restraint allegations were barred by the mandate rule; and that the horizontal claims failed as a matter of law, even if they were not barred. The court did not accept the "retail market for Brighton's women's accessories" as the relevant market, because that definition ignored the innumerable other brands that are "reasonably interchangeable in use" with Brighton products. It rejected Brighton's attempt to define Brighton as a single-brand market and held that PSKS had failed to plead a unique submarket for Brighton goods, because it had failed to first plead a "tenable dominant market."

The court also refused PSKS's second proposed market definition, which consisted of four characteristics: wholesale sale; brand-name; women's accessories; and independent retailers.

II.

We review a dismissal under rule 12(b)(6) *de novo*. *Apani Sw., Inc. v. Coca-Cola Enters., Inc.*, 300 F.3d 620, 624 (5th Cir. 2002). "To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to state a claim to relief that is plausible on its face." *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1949 (2009) (quotations omitted). The complaint need not contain "detailed factual allegations" but must state "more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do." *Bell Atl. Corp. v. Twom-*

bly, 550 U.S. 544, 555 (2007). "Where a complaint pleads facts that are 'merely consistent with' a defendant's liability, it 'stops short of the line between possibility and plausibility of entitlement to relief.'" *Iqbal,* 129 S. Ct. at 1949 (quoting *Twombly*, 550 U.S. at 557). *See generally* 2 JAMES W. MOORE ET AL., MOORE'S FEDERAL PRACTICE § 8.04[1] (3d ed. 2010).

A. Vertical price restraint claims after Leegin.

"To prove a Section 1 violation under rule of reason analysis, [plaintiffs] must show that the defendants' activities caused an injury to competition." *Doctor's Hosp., Inc. v. Se. Med. Alliance, Inc.*, 123 F.3d 301, 307 (5th Cir. 1997). Under the rule of reason, we examine the effect of the alleged restraint on competition, considering all the circumstances, "including the facts peculiar to the business and the history of, reasons for, and market impact of the restraint. . . ." *Royal Drug Co. v. Group Life & Health Ins. Co.*, 737 F.2d 1433, 1436 (5th Cir. 1984) (quotations omitted). We balance the "anticompetitive evils of a restrictive practice . . . against any procompetitive benefits or justifications within the confines of the relevant market." *Se. Med. Alliance*, 123 F.3d at 307.

PSKS argues that the Supreme Court announced a rule-of-reason standard for vertical price restraint cases that is different from the standard that has applied to vertical non-price restraint cases since *GTE Sylvania*. Specifically, PSKS claims that under *Leegin*, a plaintiff sufficiently pleads a vertical price-fixing claim just by pleading "the existence of the agreement and the scope of its operation." We need not address that contention, because, as explained in part II.B., PSKS's claim fails anyway as a matter of market definition. For the same reason, we do not need to address the argument of *amicus* American

Antitrust Institute that RPM arrangements should carry a presumption of illegality; that RPM arrangements should be treated as "inherently suspect" because they lead to higher prices or reduced output; that dual distribution systems should be presumptively illegal; and that without a presumption of illegality, the rule of reason amounts to a rule of *per se* legality for RPM.

B. The relevant market for Brighton goods and market power.

To state an antitrust claim for anticompetitive RPM, PSKS's complaint must plausibly define the relevant product and geographic markets. *See Apani*, 300 F.3d at 627. A proposed product market must include all "commodities reasonably interchangeable by consumers for the same purposes." *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 395 (1956).

> Where the plaintiff fails to define its proposed relevant market with reference to the rule of reasonable interchangeability and cross-elasticity of demand, or alleges a proposed relevant market that clearly does not encompass all interchangeable substitute products even when all factual inferences are granted in plaintiff's favor, the relevant market is legally insufficient, and a motion to dismiss may be granted.

Apani, 300 F.3d at 628.

PSKS alleged two alternative product markets, neither of which encompasses interchangeable substitute products or recognizes the cross-elasticity of demand for Brighton goods. The district court properly rejected the "retail market for Brighton's women's accessories" and the "wholesale sale of

brand-name women's accessories to independent retailers."

The court also correctly rejected the claim that Brighton products constitute their own market. In rare circumstances, a single brand of a product or service can constitute a relevant market for antitrust purposes. *Eastman Kodak v. Image Tech. Servs.*, 504 U.S. 451, 481-82 (1992). But that possibility is limited to situations in which consumers are "locked in" to a specific brand by the nature of the product. There is no structural barrier to the interchangeability of Brighton products with goods produced by competing manufacturers, nor has PSKS alleged any such structural barriers.

Nor does Brighton constitute its own submarket. Although a recognized submarket doctrine exists,[1] such markets must exist within broader economic markets. And the requirements for pleading a submarket are no different from those for pleading a relevant broader market.[2]

The second proposed market definition is similarly legally insufficient. "Wholesale sale" does not adequately define the relevant market, because the relevant market definition must focus on the product rather than the distribution level. PSKS has likewise failed sufficiently to allege why Brighton goods are

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[1] *See Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962) (stating that within broader markets, "well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes).

[2] *See H.J., Inc. v. Int'l Tel. & Tel. Corp.*, 867 F.2d 1531, 1540 (8th Cir. 1989); Staples, 970 F. Supp. at 1080 n.11.

not interchangeable with non-brand name products.[3] Nor is there any relevance to "independent retailers" to the market definition, because PSKS has not alleged facts that could establish why independent retailers do not compete with larger chain stores in the distribution of Brighton products.

Lastly, "women's accessories" is too broad and vague a definition to constitute a market. Indeed, it is impossible to imagine that Leegin could have power over such a market. As the *Leegin* court points out, 551 U.S. at 898, even anticompetitive uses of RPM do not create concern unless the relevant entity has market power. A market-power screen is thus compatible with *Leegin* and our precedent[4] and that of our sister circuits.[5] To allege a vertical restraint claim sufficiently, a plaintiff must plausibly allege the defendant's market power.

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[3] We agree with the district court that allowing PSKS to amend its complaint to correct that deficiency would be futile in light of the complaint's other flaws.

[4] *See Muenster Butane, Inc. v. Stewart Co.*, 651 F.2d 292, 298 (5th Cir. Unit A July 1981) (observing that "if a firm lacks market power, it cannot affect the price of its product, and thus any vertical restraint could not be anticompetitive at the interbrand level." (quotation omitted)).

[5] *See, e.g., Digital Equip. Corp. v. Uniq Digital Techs., Inc.*, 73 F.3d 756, 761 (7th Cir. 1996) (Easterbrook, J.) ("[S]ubstantial market power is an indispensable ingredient of every claim under the Rule of Reason."); *Assam Drug Co. v. Miller Brewing Co.*, 798 F.2d 311, 315-16 (8th Cir. 1986) (collecting cases); *Graphic Prods. Distribs., Inc. v. Itek Corp.*, 717 F.2d 1560, 1568 (11th Cir. 1983) ("We have narrowed the broad-ranging inquiry called for by the rule of reason by insisting, at the threshold, that a plaintiff attacking vertical restrictions establish the market power of the defendant." (citing *Muenster Butane*, 651 F.2d at 298)).

C. The alleged anticompetitive harm.

PSKS alleged that the RPM program forced consumers to pay "artificially" high prices for Brighton products. That claim defies the basic laws of economics. Absent market power, an artificial price hike by Leegin would merely cause it to lose sales to its competitors.

PSKS also alleged that the RPM policy deprived consumers of "free and open competition in the purchase of Brighton-brand products," because RPM limits price competition among retailers. One problem with that argument is that it ignores interbrand competition, which forces Brighton retailers to offer a combination of price and service that attracts consumers away from competing products. It also fails to recognize that retailers will cease carrying Brighton goods if Leegin imposes onerous requirements that make Brighton products difficult to sell. Moreover, robust competition can exist even in the absence of price competition. *Leegin*, 551 U.S. at 891. Retailers may seek to attract customers with better service, more knowledgeable staff, more appealing stores, and other nonprice -oriented strategies..

Nor is the termination of PSKS as a retailer an anticompetitive effect. It has been the rule since *United States v. Colgate*, 250 U.S. 300 (1919), that a manufacturer, acting unilaterally, can set resale prices and terminate non-conforming dealers. Although one circuit held that "a dealer terminated for its refusal to abide by a vertical minimum price fixing agreement suffers antitrust injury and may recover losses flowing from that termination," *Pace Elecs., Inc. v. Canon Computer Sys., Inc.*, 213 F.3d 118, 1224 (3d Cir. 2000), that holding rested on the now-rejected per se illegal treatment of resale price

maintenance, *Id.* "The purpose of the antitrust laws . . . is 'the protection of competition, not competitors.'" *Leegin*, 551 U.S. at 906 (citations omitted).

PSKS has further failed to allege any relevant factors that would indicate a plausible anticompetitive effect. Namely, PSKS has never asserted that a cartel of retailers or one dominant retailer is the "source" of Leegin's RPM program. *See H&B Equip. Co. v. Int'l Harvester Co.*, 577 F.2d 239, 245-46 (5th Cir. 1978). PSKS has claimed that Leegin is the largest single retailer of Brighton products. It is thus difficult to conceive how independent Brighton retailers could be the source of the RPM program. Nor has PSKS alleged that RPM is widespread in the relevant market, an allegation that would, in any event, contradict its claim that Brighton goods have no competition.

Even accepting PSKS's factual allegations as true, nothing in its complaint plausibly alleges a harm to interbrand competition. In *Brunswick Corp. v. Pueblo Bowl-O-Mat*, 429 U.S. 477, 489 (1977), the Court held that antitrust plaintiffs must allege and prove an injury that "reflect[s] the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation." No rule of reason can require defendants to litigate antitrust claims that do not state an antitrust injury beyond motion to dismiss. The attempt to eliminate claims that do not state an offense under the Sherman Act was at the core of *Bell Atlantic Corp. v. Twombly*, 550 U.S. at 553, and PSKS's complaint fails at that most basic level.

D. The horizontal-restraint claims.

PSKS argues that the district court erred in holding that its horizontal-restraint claims are barred by the mandate rule, which precludes litigation of waived issues on remand because they were never raised in district court. *United States v. Lee*, 358 F.3d 315, 321 (5th Cir. 2004). PSKS's attempt to plead horizontal-restraint claims for the first time in the second amended complaint mirrors previous efforts by past antitrust plaintiffs whose original claims were rejected by the Supreme Court.[6] PSKS attempted to argue its horizontal claims before the Supreme Court, but the Court explicitly refused to address the issue, because it had not been raised in the lower courts. *Leegin*, 551 U.S. at 907-08. The district court rightly dismissed the horizontal-restraint claims as barred by the mandate rule.

In any event, PSKS has not properly alleged its horizontal-restraint claims, and, irrespective of the mandate rule, the claims must be dismissed on the pleadings. As already discussed, PSKS has failed to allege that retailers were the source of the price restraint, an allegation that would have been potentially inconsistent with the complaint's factual assertion that Leegin is the largest single retailer of Brighton goods.

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[6] *See Cont'l T.V., Inc. v. GTE Sylvania Inc.*, 461 F. Supp. 1046, 1051-52 (N.D. Cal. 1978), *aff'd*, 694 F.2d 1132 (9th Cir. 1982) (foreclosing plaintiff's attempt to assert new horizontal theories on remand after the Supreme Court reversed the per se rule against nonprice vertical restraints and holding that "[s]uch a theory of Section 1 liability has never before been asserted by plaintiff and it cannot properly do so now"); *see also Omni Outdoor Adver. v. Columbia Outdoor Adver.*, 974 F.2d 502, 505-06 (4th Cir. 1992).

PSKS claims that Leegin entered into a horizontal price-fixing conspiracy by discussing special occasion discounts with its retailers in Hawaii. PSKS essentially argues that manufacturers implementing RPM cannot calibrate prices through discussions with their retailers. We cannot agree. Such a rule "can lead, and has led, manufacturers to take wasteful measures. . . . The increased cost these burdensome measures generate flow to consumers in the form of higher prices." *Leegin*, 551 U.S. at 903 (citing Brief for PING, Inc., as amicus curiae supporting petitioner). A manufacturer's discussion of pricing policy with retailers and its subsequent decision to adjust pricing to enhance its competitive position do not create an antitrust violation or give rise to an antitrust claim.

PSKS's reliance on *Toys "R" Us* for its hub-and-spoke conspiracy claim is also misguided. PSKS has not alleged that any dominant retailer imposed the RPM policy on Leegin, nor has it alleged an agreement among retailers to implement the RPM policy. In the absence of an assertion that retailers agreed to RPM among themselves, there is no wheel and therefore no hub-and-spoke conspiracy, and that allegation was therefore properly dismissed.[7]

PSKS further argues that because Leegin is a dual distributor, operating as both a manufacturer and retailer of Brighton goods, the RPM policy is a horizontal restraint. It claims that Leegin's retail presence gives it an incentive to raise retail prices through RPM in order to capture greater profits. Economic logic tells us otherwise.

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[7] Similarly off the mark is PSKS's reliance on *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305 (1956), a statutory-interpretation case that is not relevant to the issue.

Leegin participates in the retail market with nearly 5000 other stores. It must share any profit increase at the retail level with those other retailers. If Leegin sought only to raise its margins, it would raise the price of Brighton goods at the wholesale level, where it could capture all the gains. Leegin is thus no different from a manufacturer that does not have retail stores[8]; it would normally seek to minimize retailer margins as much as possible, including at its own retail stores.[9] *See Leegin*, 551 U.S. at 896.

AFFIRMED.

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[8] As the district court noted, eight other circuits have applied the traditional rule of reason to dual distribution systems. *See AT&T Corp. v. JMC Telecom, LLC*, 470 F.3d 525, 531 (3d Cir. 2006); *Electronics Commc'ns Corp. v. Toshiba Am. Consumer Prods., Inc.*, 129 F.3d 240, 243-44 (2d Cir. 1997); *Glacier Optical, Inc. v. Optique du Monde*, 46 F.3d 1141 (9th Cir. 1995) (unpublished); *Smalley & Co. v. Emerson & Cuming, Inc.*, 13 F.3d 366, 368 (10th Cir. 1993); *Hampton Audio Elecs., Inc. v. Contel Cellular, Inc.*, 966 F.2d 1442 (4th Cir. 1992) (unpublished); Ill. *Corporate Travel, Inc. v. Am. Airlines, Inc.*, 889 F.2d 751, 753 (7th Cir. 1989); *Int'l Logistics Group, Ltd. v. Chrysler Corp.*, 884 F.2d 904, 906 (6th Cir. 1989); *Ryko Mfg. Co. v. Eden Servs.*, 823 F.2d 1215, 1230-31 (8th Cir. 1987).

[9] "A manufacturer that helps dealers form a cartel is doing itself in. It will sell less, and dealers will get the monopoly profits." Easterbrook, *Vertical Restraints and the Rule of Reason*, 53 ANTITRUST L.J. 135, 142 (1984).

APPENDIX B

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 09-40506

PSKS, INC., DOING BUSINESS AS
KAY'S KLOSET . . . . KAY'S SHOES,
Plaintiff-Appellant,

versus

LEEGIN CREATIVE LEATHER PRODUCTS, INC.,
Defendant-Appellee.

Appeal from the United States District Court
for the Eastern District of Texas, Marshall

JUDGMENT

Before SMITH, GARZA, and CLEMENT, Circuit Judges.

This cause was considered on the record on appeal and was argued by counsel.

It is ordered and adjudged that the judgment of the District Court is affirmed.

IT IS FURTHER ORDERED that plaintiff-appellant pay to defendant-appellee the costs on appeal to be taxed by the Clerk of this Court.

ISSUED AS MANDATE:

APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF TEXAS
MARSHALL DIVISION

CV 2:03 CV 107 (TJW)

PSKS, INC. d/b/a KAY'S KLOSET, *et al.*
Plaintiffs.

v.

LEEGIN CREATIVE LEATHER PRODUCTS, INC.
Defendant.

MEMORANDUM OPINION AND ORDER

Before the court is Leegin Creative Leather Products, Inc.'s ("Leegin") Motion to Dismiss (Dkt. No. 152). On March 12, 2009, the court heard oral arguments on the Motion. The court has carefully considered the parties' submissions and arguments of counsel. The court GRANTS Leegin's Motion for the following reasons.

I. BACKGROUND

In *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 127 S.Ct. 2705 (2007), the Supreme Court reversed the jury verdict in plaintiff's favor in this case. In doing so, the Supreme Court changed the standard by which to judge price fixing agreements between manufacturers and the entities to whom they sell (vertical price fixing agreements). The Supreme Court announced that a "rule of reason" standard should apply to vertical price fixing agree-

ments, rather than the *per se* standard that was applied by this court. The Supreme Court remanded the case to this court to apply the "rule of reason" at retrial. This court granted the PSKS leave to file a second amended complaint (SAC) and gave the parties a briefing schedule for any Motion to Dismiss. The plaintiff has filed its amended complaint, and Leegin has filed its Motion to Dismiss.

II. LEGAL STANDARD

The legal standard for dismissing claims under FED. R. CIV. P. 12 ("Rule 12") is well established. Rule 8(a) requires that a complaint contain a "short and plain statement of the claim showing that the pleader is entitled to relief." FED. R. CIV. P. 8(a)(2). The Supreme Court has held that a complaint does not need detailed factual allegations to survive a Rule 12(b)(6) motion to dismiss, but the plaintiff's obligation to state the grounds of entitlement to relief requires "more than labels and conclusions." *Bell Atlantic Corp. v. Twombly*, 127 S.Ct. 1955, 1964-65 (2007). The factual allegations must be sufficient to raise a "right to relief above the speculative level." *Id.* at 1965. The Court must assume that the allegations in the complaint are true. *See id; Neitzke v. Williams*, 490 U.S. 319 (1989). "What Rule 12(b)(6) does not countenance are dismissals based on a judge's disbelief of a complaint's factual allegations." *Id.* at 328. The "issue is not whether [the plaintiffs] will ultimately prevail, but whether [they are] entitled to offer evidence to support [their] claim." *Jones v. Greninger*, 188 F.3d 322, 324 (5th Cir. 1999).

III. ANALYSIS

Leegin challenges PSKS's allegations as being insufficient to allege a rule of reason antitrust case.

Leegin argues that the two relevant product markets PSKS attempts to define in its SAC are untenable under antitrust law. Further, Leegin argues PSKS has not alleged facts demonstrating that Brighton has market power in the purported relevant product markets. Brighton's market power in the relevant product markets is necessary for the alleged price fixing agreement to have the requisite anticompetitive effect to be illegal in a rule of reason case. PSKS responds that it has in fact pleaded sufficiently, and the Supreme Court's opinion in *Leegin* did not require market power for a showing of an anticompetitive effect in a rule of reason analysis for vertical price fixing agreements.

In an attempt to bootstrap its case into a *per se* illegality case, PSKS added allegations in its SAC to support horizontal price-fixing and a retailer cartel. PSKS alleges that because the manufacturer in this case is also a distributor and retailer, the pricing agreement is horizontal as well as vertical. Additionally, PSKS alleges the conduct amounts to a classic hub and spoke conspiracy. Leegin makes two arguments for dismissing PSKS's horizontal allegations from its SAC. First, Leegin argues that because PSKS did not originally proceed on a horizontal theory, it is precluded from doing so now. Second, Leegin argues, PSKS's horizontal restraints theories fail as a matter of law.

A. Relevant Product and Geographic Market

The first step in a rule of reason analysis is determining the relevant market. *Apani Southwest Inc. v. Coca-Cola Enterprises Inc.*, 300 F.3d 620, 627 (5th Cir. 2002). "Proof that the defendant's activities, on balance, adversely affected competition in the appropriate product and geographic markets is

essential to recovery under the rule of reason." *Hornsby Oil Co. V. Champion Spark Plug Co.*, 714 F.2d 1384, 1392 (5th Cir. 1983). A relevant product market includes the line of goods or services reasonably interchangeable in use. *United States v. E.I. duPont deNemours & Co.*, 351 U.S. 377, 396 (1956). The relevant geographic market "is the area of effective competition . . . in which the seller operates, and to which the purchaser can practicably turn for supplies." *Tampa Elect. Co. v. Nashville Coal Co.*, 365 U.S. 320, 327 (1961). The Fifth Circuit requires plaintiffs to define their market with reference to the rule of reasonable interchangeability. *Apani*, 300 F.3d at 628. Where "the relevant market is legally insufficient . . . a motion to dismiss may be granted." *Id.* at 627.

1. Relevant Product market

A relevant product market includes the line of goods or services reasonably interchangeable in use. *United States v. E.I. duPont deNemours & Co.*, 351 U.S. at 393. "Determination of the competitive market for commodities depends on how different from one another are the offered commodities in character or use, how far buyers will go to substitute one commodity for one another." *Id.* "[I]t is the use or uses to which the commodity is put that control." *Id.* at 396.

PSKS alleges two product markets in its SAC. The first is "retail market for Brighton's women's accessories." SAC ¶ 24. The second is the "wholesale sale of brand-name women's accessories to independent retailers." SAC ¶ 24. Leegin argues that neither market is tenable under current law.

i. "Retail market for Brighton's women's accessories"

Leegin first argues that the market definition "retail market for Brighton's women's accessories" fails because countless brands are "reasonably interchangeable in use" with Brighton's products. Dfts. MTD at 7. Indeed, courts have regularly held that a single brand, no matter how distinctive or unique, cannot be its own market. *Little Ceasar Enterprises, Inc. v. Smith*, 34 F.Supp. 2d 459, 477 n.30 (E.D. Mich. 1998) (collecting cases). "Even where brand loyalty is intense, courts reject the argument that a single branded product constitutes a relevant market." *Green Country Food Market, Inc. v. Bottling Group, LLC*, 371 F.3d 1275, 1282 (10th Cir. 2004). The Fifth Circuit has held that "absent exceptional market conditions, one brand in a market of competing brands cannot constitute a relevant product market. *Domed Stadium Hotel, Inc. v. Holiday Inns, Inc.*, 732 F.2d. 480, 488 (5th Cir. 1984)

PSKS attempts to circumvent the law by arguing that the SAC alleges special factors that could make the "retail market for Brighton's women's accessories" a unique submarket that should be considered separately for antitrust purposes. Pls. Reply at 8. Indeed, "antitrust law recognizes . . . economically significant submarkets . . . which themselves constitute relevant product markets." *Domed Stadium Hotel, Inc. v. Holiday Inns, Inc.* 732 F.2d 480, 487-88 (5th Cir. 1984). PSKS points out that "[t]he fact finder may determine a submarket exists by 'examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct

customers, distinct prices, sensitivity to price changes, and specialized vendors." *Id.* (citing *Brown Shoe v. U.S.*, 370 U.S. 294, 325 (1962)).

PSKS, however, has failed to allege a tenable dominant market to its alleged submarket. PSKS attempts to argue there can be some submarket without a tenable dominant market. Further, PSKS ignores that a submarket is still a "market." While PSKS may have pleaded facts sufficient to define a submarket, that alone will not get PSKS past the clear law that a single brand cannot be its own market. *See id.* There is no law supporting PSKS's apparent position that submarkets are exempt from the law requiring a market to constitute more than a single brand. "Retail market for Brighton's women's accessories," therefore, is not a tenable product market under the law.

ii. "Wholesale sale of brand-name women's accessories to independent retailers"

Next, PSKS argues that "wholesale sale of brand-name women's accessories to independent retailers" is a relevant product market. Leegin argues that this alternative product market fails because it excludes products reasonably interchangeable with Brighton's products. Leegin breaks down into different components what it calls the "gerrymandered" product market: 1) wholesale sale, 2) brand-name 3) women's accessories, and 4) independent retailers.

First, as Leegin points out, "wholesale sale" is inappropriate because it does not focus on how any agreement impacts consumers. Relevant markets must be defined in terms of the product itself without regard to the distribution level. *See, e.g., Assam Drug Co. Inc. v. Miller Brewing Co., Inc.*, 798 F.2d 311 (8th

Cir. 1986) (relevant market was the "interbrand beer market" not limited to the wholesale market); *R.D. Imports Ryno Indus. v. Maza Distrib.* 807 F.2d 1222, 1225 (5th Cir. 1987) (relevant market was cars, foreign and domestic, that consumers viewed as substitutes with no limitation to wholesale market).

PSKS attempts to circumvent this law by arguing the Supreme Court distinguished the "effect that this type of constraint poses for manufacturer cartels." For example, PSKS argues "by imposing a fixed margin, manufacturers can easily police competing manufacturer sales and more easily fix wholesale prices. . . The economic injury of this activity falls not only on the consumer, who is charged more than a competitive price for the goods, but also on those dealers purchasing their goods at wholesale." Dfts. Resp. at 5. However, PSKS has failed to define the relevant market in terms of the product itself and not the distribution level of the product. This must be done without regard to how the wholesale market is affected. Therefore, "wholesale market," adds nothing to PSKS's alternative product market.

Second, Leegin argues that including "brand name" in the product market definition is wrong, because it is consclusory and unsupported by any facts. Leegin cites to *Star Tobacco, Inc. v. Darilek*, 298 F.Supp 2d 436, 446 (E.D. Tex 2003) granting a Motion to Dismiss because the plaintiff had failed to allege facts supporting "brand name" and "discount" or "generic" cigarettes were not interchangeable. The *Star Tabacco* court held "[b]ecause Defendant's counterclaim fail[ed] to make any factual allegations to the effect that discount cigarettes and branded cigarettes are not interchangeable, Defendants have submitted an inadequate pleading." *Id.*

PSKS responds that including "brand name" does add something to the purported product market. *See Babyage.com Inc. v. Toys "R" Us, Inc.*, 558 F.Supp.2d 575 (E.D.Pa. 2008) (allowing products to be defined by "high-end baby and juvenile strollers"). *Babyage* is distinguishable from the case at bar, however. In *Babyage*, the plaintiff had pleaded why "high-end" baby strollers were not interchangeable with other types of strollers. *Id.* Here, PSKS fails to allege facts that support "brand names" are important to interchangeability in this case. PSKS fails to allege facts that would support a showing that consumers in the market for "brand name" women's accessories, whatever those accessories are, may only turn to other brand-name products. All of PSKS's facts are couched in terms of why the "Brighton" brand is unique and high end. As already discussed, a single brand can not be its own market. *See Domed Stadium*, 732 F.2d at 487-88. It is plausible that PSKS would be able to amend its complaint to allege facts necessary to support an allegation that "brand name" accessories are important to its product definition. However, granting leave to do so would be in vain, because alleging such facts would not be enough to salvage the case in light of the its other deficiencies.

"Women's Accessories," Leegin argues, is not an appropriate product market because it groups together products that are not interchangeable with each other. In a sister case to this one, Judge Greer in the Eastern District of Tennessee held "picture frames do not compete with women's handbags and shoes do not compete with jewelry." *Spahr v. Leegin*, 2008 WL 3914461, at *9 n.3. This court agrees. "Women's accessories" is too broad and vague to constitute a market.

Lastly, Leegin argues, including "independent retailers" is in error, because it inappropriately limits the relevant market to a subset of retailers. Leegin argues that "independent retailers" lacks specificity, therefore, leaves the relevant market too vague to be a tenable definition. Further, Leegin argues, to the extent "independent retailers" is intended to describe some subset of retailers, such as stores like PSKS, the complaint fails to allege why it should be so limited. The court agrees. PSKS has cited no law or support as to how defining the market in the bounds of "independent retailers," no matter what they are, makes the alternative product market tenable. Relevant product markets include goods that are reasonably interchangeable in use. *E.I. du Pont deNemours & Co.*, 351 U.S. at 393. PSKS has failed to allege the interchangeability, or lack thereof, between one subset of retailers and other retailers selling exactly the same products. *See Apani*, 300 F.3d at 628.

2. Geographic Market

The relevant geographic market "is the area of effective competition . . . in which the seller operates, and to which the purchaser can practicably turn for supplies." *Tampa Elect. Co. v. Nashville Coal Co.*, 365 U.S. 320, 327 (1961). PSKS alleges that it purchases most of its products from the Dallas Market (SAC ¶7) and alleges a product market of the greater Dallas area. SAC ¶24. Because, as discussed above, the wholesale market cannot be the relevant product market, the geographic area where PSKS purchases its products is irrelevant. Leegin does not "concede that [the Greater Dallas Area] is appropriate for the retail sale market; however, it is not moving to dismiss on these grounds." Dfts. MTD at 11 n. 4. "The Greater Dallas area" may be a tenable geographic

market for the retail sales of Brighton Products. However, that matters little in that PSKS has not pleaded a tenable product market.

B. Anticompetitive Effect

Leegin also argues that PSKS's failure to allege anticompetitive effects provides further reason for dismissing the case. The parties dispute whether the Supreme Court intended that a showing of a defendant's market power is a requisite for finding that a vertical price fixing agreement has an anticompetitive effect. The court need to reach this issue, however. Because PSKS has not defined a relevant market, the court cannot assess the alleged price fixing agreement's anticompetitive effect.

C. Addition of Horizontal Restraint Theories

PSKS attempts to allege facts supporting a horizontal price fixing agreement and a horizontal hub and spoke conspiracy, both of which are illegal *per se*. PSKS's horizontal theories are based on the fact that Leegin is also a distributor of its own products. Leegin argues these new theories are barred because they were not raised in the original jury trial, the facts PSKS allege are still analyzed under the rule of reason, and the alleged facts fall short of supporting a cartel.

1. The Mandate Rule

PSKS cannot now plead a horizontal restraint case that it failed to raise in the original trial. The Mandate Rule "bars litigation of issues decided by the district court but foregone on appeal or otherwise waived, for example because they were not raised in the district court." *U.S. v. Lee*, 358 F.3d 315, 321 (5th Cir. 2004).

PSKS cites to *Castellano v. Fagozo*, 352 F.3d 939 (5th Cir. 2003) for the proposition that when a higher court changes well established precedent, a party may pursue a claim it did not raise in the lower court out of non-necessity. In *Castellano*, the Fifth Circuit changed the law regarding the elements of a number of the plaintiff's federal claims such that a malicious prosecution claim previously asserted by the plaintiff was no longer redundant of his federal claims. On remand, the Fifth Circuit ordered that the plaintiff could re-file and pursue his malicious prosecution claim, despite the fact that he had previously voluntarily dismissed the claim. *Id.*

The case at bar is different from *Castellano*, however. Here, the Supreme Court did not specifically allow PSKS to re-plead allegations it had previously abandoned. First, the horizontal allegations were never raised in the original trial. Second, the Supreme Court did not mention what PSKS could plead on remand. More analogous to this case is *Continental TV, Inc. v. GTE Sylvania Inc.*, 461 F.Supp. 1046 (N.D. Cal. 1978), *a f'd* 694 F.2d 1132 (9th Cir. 1982). In *Continental*, the district court did not allow the plaintiff to plead horizontal allegations after the Supreme Court overruled *per se* illegality for the restraint at issue, and remanded the case to be tried under the rule of reason. *Id.* at 1051-52. In this case, nothing prevented PSKS from raising its horizontal agreement and conspiracy allegations in the original trial, and it cannot do so now.

2. Dual Distributorship Situations

Even if the court were to allow PSKS to plead it its horizontal restraint allegations, those allegations fail as a matter of law. Where a manufacturer is both a wholesale distributor and retail distributor it is

called a "dual distribution system." *Red Diamond Supply, Inc. v. Liquid Carbonic Corp.*, 637 F.2d 1001, 1004-1007 (5th Cir. 1981). Restraints in "dual distribution systems" are analyzed under the rule of reason. *Id.* The Fifth Circuit has held that in situations like Leegin's, where the manufacturer also distributes some of its own goods, restraints are properly analyzed under the rule of reason. *Id.* Eight other circuits have reached the same result.[1] PSKS argues that those cases are distinguishable because they did not deal with price fixing agreements, but instead dealt with other types of restraints.

PSKS urges that in this type of "dual distribution setting," where the restraints are price fixing agreements, "the natural checks and balances provided by the countervailing interests of manufacturer/consumer against those of the retailer as to retail and retail margins simply are not present." Pls. Response at 16. PSKS relies on *United States v. McKesson & Robbins, Inc.*, 351 U.S. 305 (1956) to support its

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[1] *See, e.g., AT & T Corp. v. JMC Telecom, LLC*, 470 F.3d 525, 531 (3d Cir. 2006) (agreement involving dual distributor arrangement remained "vertical" and analyzed under the rule of reason); *Electronics Communications Corp. v. Toshiba America Consumer Products, Inc.*, 129 F.3d 240, 243 (2d Cir. 1997) (same); *Glacier Optical, Inc. v. Optique du Monde*, 46 F.3d 1141 (9th Cir. 1995) (not for publication) (same); *Smalley & Co. v. Emerson & Cuming, Inc.*, 13 F.3d 366, 368 (10th Cir. 1993) (same); *Hampton Audio Electronics, Inc. v. Contel Cellular, Inc.*, 966 F.2d 1442 (4th Cir. 1992), as amended, (Aug. 6, 1992) (same); *Ill. Corporate Travel, Inc. v. Am. Airlines, Inc.*, 889 F.2d 751, 753 (7th Cir. 1989) (same); *International Logistics Group, Ltd. v. Chrysler Corp.*, 884 F.2d 904, 906 (6th Cir. 1989); *Ryko Mfg. Co. v. Eden Services*, 823 F.2d 1215, 1230, 92 A.L.R. Fed. 387 (8th Cir. 1987), (same).

position. In *McKesson*, the defendant, a manufacturer and wholesale distributor, had entered price fixing agreements with other competing wholesale distributors of products manufactured by the defendants. Because the defendant participated as a wholesaler and manufacturer in the market, the court held the agreements in question were between "firms [or] corporations in competition with each other." As the Tennessee court pointed out, however, PSKS's reliance on *McKesson* is misplaced. *Spahr* at *6. "The issue before the Supreme Court was one of statutory interpretation . . . [it] did not address or discuss wether the restraints at issue were horizontal or vertical for Sherman Act purposes and its analysis has little, if any, application to the issue before the Court." *Id.*

The law in the Fifth Circuit is that these types of arrangements are dual distributorships and should be analyzed under the rule of reason. *Red Diamond Supply* 637 F.2d at 1004-1007. The *Red Diamond* court did not distinguish between price fixing and other types of restraints. Therefore, the same deficiencies in the rule of reason analysis above are present in PSKS's dual distributorship case.

3. Hub and Spoke Conspiracy

PSKS next attempts to have its case fit into a *per se* analysis by arguing it has pleaded facts showing that Leegin's price fixing activities are in furtherance of a "hub and spoke" retailer cartel.

> "A hub and spoke conspiracy involves a hub, generally the dominant purchaser or supplier in the relevant market, and the spokes, made up of the distributors involved in the conspiracy. The rim of the wheel is the connecting agreements

> among the horizontal competitors (distributors) that form the spokes. Each of the three parts is integral in establishing a *per se* violation under the hub and spoke theory."

Total Benefits Planning Agency, Inc. v. Anthem Blue Cross and Blue Shield, 552 F.3d 430, 435 n.3. "The critical issue for establishing a *per se* violation with the hub and spoke system is how the spokes are connected to each other . . ." *Id.* at 436. PSKS argues it "intends to prove that there are a series of agreements between Leegin and independent retailers to fix prices of Brighton goods (spoke); that Leegin's independent retailers have formed a cartel with each other and with Leegin as a retailer to prevent discounting and price competition (wheel); that in response to pressure from retailers involved in the cartel, Leegin has enforced its price fixing agreements against discounters to stamp-out price competition (hub); that retailers have discussed and indeed come to agreements as to the terms of the price fixing agreements and exceptions thereto (wheel)." Pls. Response at 12-13. In analyzing the complaint in *Spahr*, the court explained:

> There is no allegation by plaintiffs here that retailers have agreed to fix prices and then compelled the manufacturer, Leegin, to utilize resale price maintenance. In fact, plaintiffs have affirmatively alleged the opposite, *i.e.*, that Leegin coerced retailers and forced upon retailers the resale price maintenance agreements.

Spahr, at *12.

It appears that PSKS has attempted to resolve this deficiency in its SAC in this case by adding the following paragraph (14):

> Brighton would, following the suggestion and concurrence of retail dealers, from time to time amend the Policy. One such instance occurred in January 2003, when Brighton invited some of its most successful retail dealers to Hawaii. One topic discussed at this conclave of retailers was the Brighton pricing policy. *A consensus of the retailers was reached, and the result of that meeting resulted in a policy being announced*: "What we have decided is OK after talking to more than 100 retailers is a birthday Club that on your birthday (or within a short time of your birthday) a consumer can get a discount on 1 piece of merchandise in your store (everything not only Brighton)."

This addition, however, is insufficient to properly plead a hub and spoke conspiracy. There is no allegation that retailers agreed to the alleged RPM among themselves. The allegations suggest not a retailer cartel, but that Leegin's interests were the driving force behind the program. PSKS argues that a jury could infer that because these retailers arrived at a consensus as to an exception to the pricing policy, they discussed the pricing policy in more detail, discarded various other proposals for exceptions to the policy, and agreed to maintain the policy as a whole. This argument is unpersuasive, however.

PSKS must *allege* an agreement among the retailers. Rule 8 "requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do." *Twombly*, 127 S.Ct. at 1965. In *Twombly*, the Supreme Court rejected an antitrust claim because the horizontal conspiracy was alleged without the level of detail-the who, what, when, where, and how. Here, PSKS has likewise

failed to allege what is necessary, and there is no evidence that there are facts that would support such a claim. Without those facts, PSKS is missing the requisite wheel in the classic hub and spoke arrangement.

D. State Law Claims

PSKS alleges that Brighton also violated Texas Business and Commerce Code § 15.05 *et seq*. SAC 34. Leegin argues that PSKS cannot now bring this cause of action because it already abandoned those claims before the previous trial. PSKS does not respond to Leegin's argument. PSKS's state law claims, therefore, are dismissed.

IV. CONCLUSION

PSKS has not pleaded a tenable product market for a rule of reason analysis. PSKS cannot now bring horizontal restraint claims it never brought in the original trial in this case. Regardless of whether the court allows PSKS to add allegations to its SAC which support its horizontal restraints theories, those theories also fail as a matter of law. PSKS has likewise abandoned its state law claims in this case. Leegin's Motion to Dismiss is GRANTED.

SIGNED this 6th day of April, 2009

/s/ T. John Ward
T. John Ward
United States District Judge

APPENDIX D

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF TEXAS
MARSHALL DIVISION

Civil Action No. 2:03-CV-107-TJW

PSKS, INC. D/B/A KAY'S KLOSET . . . KAY'S SHOES; AND TONI COCHRAN, L.L.C., D/B/A TONI'S
Plaintiffs,

v.

LEEGIN CREATIVE LEATHER PRODUCTS, INC.
Defendant.

SECOND AMENDED COMPLAINT

For its causes of action against Defendant LEEGIN CREATIVE LEATHER PRODUCTS, INC., PSKS, INC. D/B/A KAY'S KLOSET . . . KAY'S SHOES, states and alleges as follows:

I.
Parties

1. Plaintiff PSKS, Inc. d/b/a Kay's Kloset . . . Kay's Shoes ("Kay's Kloset") is a corporation duly organized and registered in accordance with Texas law.

2. Defendant Leegin Creative Leather Products, Inc. ("Leegin") is a California Corporation. Defendant may be served with process by serving its registered agent, Jerry Kohl at 14022 Nelson Ave., Industry, California 91746.

II.
Jurisdiction

3. This Court has jurisdiction in this case under 28 U.S.C. §1331, 28 U.S.C. §1337, and28U.S.C. §1367. This Court also has jurisdiction in this case as it involves a federal question. More specifically the case involves the Sherman Anti-Trust and Clayton Acts.

4. The court has jurisdiction over the state law claims by virtue of supplemental jurisdiction pursuant to 28 U. S.C. § 13 67.

III.
Venue

5. Venue of this case is appropriate in the Eastern District of Texas under 15 U.S.C. §15(a). More specifically, Defendant is doing business in the Eastern District and has agents in the Eastern District. Additionally, venue of this case is appropriate in the Eastern District of Texas under 28 U.S.C §1391(b) and (c). Leegin has sufficient contracts with this district to subject it to personal jurisdiction. In fact, numerous retail stores, including ladies' boutiques, sell Brighton products supplied by Defendant Leegin. Further, the Brighton Ladies Division Manager for Defendant Leegin is Laura Young, who resides in Tyler, Texas. She has regional and/or national responsibility for Defendant Leegin, was a significant party to transactions involving Defendant Leegin and the Plaintiff Kay's Kloset, and on information and belief, at all natural times acted in the course and scope of her employment.

IV.
Facts of the Case

6. During the operative time at issue, Plaintiff PSKS, Inc., did business as Kay's Kloset . . . Kay's Shoes in Lewisville, Texas. Kay's Kloset was a retail store for fashions, shoes and accessories. For a number of years, it was a retail store for "Brighton" products, a line of handbags, belts, jewelry and accessories manufactured by Defendant Leegin. It was instrumental in introducing Leegin's Brighton line of products to the market Kay's Kloset serves. Over the course of the years, these products have accounted for a substantial portion of Plaintiff's business, and in the last 36 months that Plaintiff bought and sold Brighton products, those products accounted for approximately $1,500,000 or more in retail sales.

7. Kay's Kloset principally served customers in the greater Dallas market area. It primarily acquired its products from manufacturers and distributors who offered those products to independent retail stores at the Dallas Market. It competed with other independent retail stores, which also primarily obtained their goods offered for resale from manufacturers and distributors that sold at periodic shows at the Dallas Market.

8. In the early 1990's, Leegin began to manufacture the Brighton brand of products, which it markets as its signature product. Leegin distributes the Brighton line in two primary methods. It sells to independent retailers directly. It does so by showcasing its merchandise at period product shows at the Dallas Market center and at other product shows at certain other market centers. By virtue of its presence at the Dallas Market, it has recruited many retailers and established its brand as a dominant

brand for independent retailers of women's accessories to offer. The other manner of distributing these products is through stores directly owned or controlled by Leegin, its divisions or subsidiaries, or its owner.

9. Defendant Leegin has, at material times, had a retail pricing and promotional policy to eliminate or suppress price competition among retailers of Brighton products. Leegin fixed suggested retail prices ("SRP") for the Brighton line through a so-called "Retail Pricing and Promotion Policy." A copy of this Policy, as it existed during a portion of the time, is attached hereto as exhibit "A." This Policy solicits agreement from retailers not to discount Brighton products, permitting discounts only when agreed to in writing by Jerry Kohl, the owner of Leegin, or Laura Young, Ladies Division Sales Manager.

10. Leegin also entered into a series of contracts with its independent retail stores. Beginning in 1998, it formed a program called the "Heart Store" program. Certain selected "Brighton" retail dealers were invited to participate in this program. Under the terms of the program, these Brighton retail dealers were provided incentives, in the form of payment terms, sales assistance, and other benefits for agreement to the terms of participating in the program. To join the program, retail dealers were required to execute and return a form that demonstrated its agreement to participate. One of the terms of participation was that the retail dealer agreed to adhere to the Brighton retail pricing policy, or that it sell only at the suggested price.

11. Brighton provided certain products pursuant to other contracts. One such contract was the "Luggage Agreement." One of the provisions of that

contract was that the Brighton luggage would be sold only at the Brighton fixed retail price.

12. Brighton entered into franchising contracts with a number of franchisees. Those franchisees agreed in the franchise contract to certain terms, one of which was an agreement to sell Brighton goods only pursuant to the Suggested Brighton policy.

13. After Leegin introduced its "Retail Pricing and Promotion Policy" and "Heart Store" programs, and at the insistence of many of its most faithful retail dealers, Leegin made changes to the language of the "Retail Pricing and Promotion Policy", began to enforce the Policy with greater regularity and began to respond to complaints from its retail dealers regarding discounting retailers with greater levels of enforcement.

14. Brighton would, following the suggestion and concurrence of retail dealers, from time to time amend the Policy. One such instance occurred in January 2003, when Brighton invited some of its most successful retail dealers to Hawaii. One topic discussed at this conclave of retailers was the Brighton pricing policy. A consensus of the retailers was reached, and the result of that meeting resulted in a policy being announced: "What we have decided is OK after talking to more than 100 retailers is a birthday Club that on your birthday (or within a short time of your birthday) a consumer can get a discount on 1 piece of merchandise in your store (everything not only Brighton)."

15. Brighton frequently intervened to reconcile pricing disputes between competing retailers of Brighton who were competing. As a Defendant sales representative disclosed to Phil Smith, Defendant's

management would "try to work up some agreement from the middle man. I mean, maybe this would blow up and * * * they'll discuss it with [one retailer]. They'll discuss it with the [other retailer], you know, make everybody play by the rules." In this manner, Brighton would act as the hub in a classic spoke and hub horizontal price fixing conspiracy.

16. Leegin products are differentiated from other products by virtue of carrying the "Brighton" brand. On its website, Leegin acknowledges and boasts of how it is different from other products:

> Today Brighton is the only major accessories line featuring products that coordinate from head to toe. A customer might choose a lipstick case that matches a wallet, jewelry that matches a pair of sunglasses, a handbag that matches her footwear, or an entire coordinating collection consisting of multiple accessories.
>
> The company prides itself on the "Brighton Difference," which is rooted in the philosophy that the difference is in the details.

17. Because Leegin offers products that are highly differentiated, it has market power.

18. Leegin also has market power because it occupies a dominant position as supplier to independent women's specialty stores. It occupies the single largest show room at market; it is able to disrupt other sales efforts by offering extensive product seminars; it is viewed as the preferred supplier to stores offering women's accessories because of the selection and nature of the product offerings, and the fact that it has decided to offer its products through a large network of independent retailers. It is, in fact,

the largest supplier of women's accessories to distribute its goods through such a network.

19. Leegin took many and frequent steps to maintain its market power and to discourage competitors and potential competitors from competing with the Brighton product. These steps included: (a) broadly and vigorously asserting tradedress/trademark infringement cases against other manufacturers who sought to offer competing products; (b) requiring retailers to carry minimum levels of product, so as to limit and foreclose the ability of those retailers to offer competing goods; (c) refusing to sell to retail dealers that carry certain competing product lines; and (d) exercising its dominant position in the Dallas market to discourage traffic to other distributors at certain times.

20. Beginning in late Fall 2002, and continuing thereafter, Leegin began to enforce the SRP policy against Kay's Kloset, attempting to secure agreement from Plaintiff to comply with the policy, while at the same time receiving agreements from other retailers to adhere strictly to Leegin's pricing policy. In conversations trying to secure Plaintiff's agreement to adhere to the policy, Brighton's sales representative was asked whether a competitor of the Plaintiff had agreed to the policy. Plaintiff was assured that the competitor had agreed to the policy, and that the competitor no longer would be discounting Brighton products.

21. Plaintiff, Kay's Kloset, had, at certain times, offered to its customers 20% off Leegin-related products to directly compete within Plaintiff's market. Leegin demanded that signs promoting the sale be removed, and threatened sanctions of loss of the Leegin product line. As stated by Leegin's sales

representative, Jan Clinkscale, told the owners of Kay's Kloset: "When people discount, it always comes back to haunt them. We don't want people to discount — we want people to sell Brighton at regular price." When Plaintiff refused to adhere to the SRP, Leegin stopped shipping products to Kay's Kloset. At the time that Plaintiff was informed of the action taken by Leegin, Plaintiff was told that the action was subject to review if Plaintiff would indicate agreement to adhere to the SRP in the future.

22. Defendant and its retail dealers have deliberately set up an unlawful retail pricing policy which Defendant enforces to unreasonably restrain prices. Defendant's actions reduce competition. Its conduct exploits its market power in the provision of women's accessories to independent retail stores in the Dallas market area, and it exploits the market power it has by offering branded products that are highly differentiated from other products. By enforcing independent retailers to agree not to discount, Defendant can insulate the retail stores it owns or controls from price competition and protect retailers who have cartelized from price competition from more innovative and efficient retailers.

23. As a result of the Plaintiff's attempting to exercise its protected right to compete, and because it chose to offer products at prices below those mandated by Leegin, Leegin deliberately punished Plaintiff and cut off all future purchases of Leegin-related products. As a result of Leegin's termination of sales to Plaintiff of Brighton goods, Plaintiff was no longer able to operate a profitable retail business and has been forced to close its store.

24. The relevant product markets at issue in this case are: (a) the wholesale sale of brand-name women's accessories to independent retailers; and (b) the retail market for Brighton women's accessories. The relevant geographic market is the greater Dallas, Texas area. At all relevant times up to and including the present, Defendant had a substantial market power in the relevant product and geographic market.

25. Brighton-brand products are unique. Many customers do not consider other accessories suitable substitutes for their use of Brighton-brand products, nor would they substitute other accessories for Brighton-brand products, nor would they do so even in response to a significant, non-transitory increase in the price of Brighton-brand products.

26. Brighton-brand products are distinct products characterized by an inelasticity in demand, and little cross-elasticity of demand between Brighton-brand products and demand for competing products.

27. The purpose, effects, tendency, or capacity of the acts and practices described herein lessened or tended to lessen competition in the relevant market. Specifically, the course of conduct charged herein had the following effects, among others:

a. Prices paid by consumers of Brighton-brand products were maintained at artificially high and anti-competitive levels;

b. Consuming members of the public were deprived of free and open competition in the purchase of Brighton-brand products;

c. Plaintiff was hindered in its ability to acquire competing products; and

d. Members of the consuming public were forced to pay artificially high, anti-competitive prices for Brighton-brand products.

Causes of Action

28. *Anti-Trust Violations*: Defendant has committed anti-competitive acts in violations of the federal and state anti-trust laws. Defendant Leegin is a manufacturer, distributor, and retailer of the Brighton line of accessories. Plaintiff was a retailer of Brighton products with Defendant. The Brighton products affect interstate commerce in that the product line is sold and used throughout the country.

29. Defendant has engaged in a price fixing scheme for the Brighton line of products that is illegal *per se*. At all times pertinent hereto, Defendant operated as a retailer of Brighton-brand products, and agreed with other retailers of Brighton-brand products on the price at which those goods would be sold to the consuming public. Those agreements, constitute horizontal cartel activities and constitute per se violations of the Sherman Antitrust and Clayton Acts.

30. Plaintiff was injured in its business and property by the Defendant's enforcing this illegal agreement against it, and refusing to sell to Plaintiff. As a result of these illegal agreements, and the Defendant's conduct, Plaintiff is entitled to treble damages.

31. Defendant's conduct also is a violation of the antitrust laws, in that it constitutes an unreasonable restraint on trade under the rule-of-reason, as that rule was described by the United States Supreme Court in this case. The conduct at issue in this case harmed the actual and potential competition in the

above-described markets. The products at issue do not require service, instruction, or other post-sale aspects that would be likely to be underprovided in the absence of a pricing restriction; the use of pricing restrictions in this case serve to restrict and does not enhance entry into the market; to the extent that any services are required to be offered by retailers, those services could be required directly, such that the incentives created by a price fixing scheme are not a more efficient means of achieving the results; the price fixing scheme facilitates the organization and operation of a retail cartel in the sale of these goods; and, the Defendant exercises its market power to limit or discourage the sales by stores of products by new entrants.

32. Brand-named women's accessories, and especially the area of handbags, can be characterized by the wide-spread adoption of practices that have the effect of limiting price competition among competing brands. Because of the lack of price competition among competing products, the effect of the price fixing practices of the Defendant results in consumers paying more and harm to those consumers.

33. For these various reasons, the price fixing scheme practiced by the Defendant is anticompetitive, and violates the Sherman and Clayton Acts.

34. Defendant has also violated Texas Business and Commerce Code § 15.05, *et seq.*, relating to monopolies, trusts, and conspiracies in restraint of trade. Defendant has committed the unlawful practices as described above, including: a) entering into a contract, combination, or conspiracy in restraint of trade or commerce; b) monopolizing, attempting to monopolize, or conspiring to monopolize trade or

commerce; and/or c) selling, leasing, or contracting for the sale or lease of goods for use, consumption, or resale, or to fix a price for such use, consumption, or resale, or to discount from or rebate upon such price, on the condition, agreement, or understanding that the Plaintiff would not be permitted to sell Brighton products without conforming to a price fixing scheme, where the effect of the condition, agreement, or understanding may be to lessen competition substantially in trade or commerce.

35. As a consequence of Defendant's actions, Plaintiffs have suffered injury in the form of prospective lost profits, and are entitled to actual and treble damages. Defendant has taken actions to hurt the value and market share of Plaintiffs' retail business to the benefit of Defendant. As a result of Defendant's actions, Plaintiffs have suffered injury and are entitled to actual and treble damages in accordance with the federal and state anti-trust statutes.

WHEREFORE, ON THE ABOVE PREMISES, Plaintiffs respectfully requests, after trial of this cause, that Plaintiff be awarded; a) actual damages; b) treble damages; c) attorney's fees and costs; and d) all other relief to which Plaintiffs may be justly entitled, including equitable relief necessary to protect Plaintiffs' interest and/or to reinforce the applicable protection of federal and state law.

DEMAND FOR JURY TRIAL

PSKS, Inc., demands a jury trial on all issues so triable.

Dated: December 29, 2008

Respectfully submitted,

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ATTORNEYS FOR PLAINTIFF

APPENDIX E

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF TEXAS
MARSHALL DIVISION

Civil Action No. 02-03CV-107TJW

PSKS, INC. D/B/A KAY'S KLOSET . . . KAY'S SHOES; AND TONI COCHRAN, L.L.C., D/B/A TONI'S
Plaintiffs,

v.

LEEGIN CREATIVE LEATHER PRODUCTS, INC.
Defendant.

First Amended Complaint Excerpts

* * * *

9. In the early 1990's Leegin began to manufacture the Brighton brand of products, which it markets as its signature product. Leegin distributes the Brighton line through thousands of independent retailers, as well as through stores directly owned or controlled by Leegin or its owner.

* * * *

18. Defendant has also violated the anti-trust laws in that it has entered into agreements with retailers to charge only those prices fixed by Leegin. If a retailer refuses to enter into such an agreement, or if after agreeing to such a price fixing scheme, violates the agreement, Leegin deliberately withdraws their

products from price competing retailers such as the Plaintiffs, at the request of and/or in combination with each other and competing retailers as part of a conspiracy to protect the other retailers from price competition and protect the suggested retail prices of Defendant.

* * * *

Respectfully submitted,

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